(1)

No. 96-7185-CFY
Status: GRANTED

Title: Garrit Bates, Petitioner
v.
United States

Docketed:
December 23, 1996

Court: United States Court of Appeals for the Seventh Circuit

Counsel for petitioner: Oren,C. Richard

Counsel for respondent: Solicitor General

Entry	Date	Note	Proceedings and Orders
1	Dec 18 1996	G	Petition for writ of certiorari and motion for leave to proceed in forma pauperis filed. (Response due January 22, 1997)
3	Jan 16 1997		Memorandum of respondent United States in opposition filed.
4	Jan 30 1997		DISTRIBUTED. February 14, 1997 (Page 45)
6	Feb 18 1997		Petition GRANTED. SET FOR ARGUMENT October 7, 1997. **********
7	Mar 6 1997	G	Motion of petitioner for appointment of counsel filed.
9	Mar 6 1997		Order extending time to file brief of petitioner on the merits until April 25, 1997.
10	Mar 10 1997		DISTRIBUTED. March 14, 1997 (Page 28)
11	Mar 17 1997		Motion for appointment of counsel GRANTED and it is ordered that C. Richard Oren, Esquire, of Rochester, Indiana, is appointed to serve as counsel for the petitioner in this case.
12	Apr 11 1997		Joint appendix filed.
13	Apr 25 1997		Brief amicus curiae of National Association of Criminal Defense Lawyers filed.
14	Apr 25 1997		Brief of petitioner Garrit Bates filed.
16	May 16 1997		Order extending time to file brief of respondent on the merits until June 13, 1997.
17	Jun 13 1997		Brief of respondent United States filed.
18	Jul 24 1997		Reply brief of petitioner filed.
19	Jul 28 1997		CIRCULATED.
20	Aug 19 1997		Record filed.
		*	Record proceedings U.S.C.A. Seventh Circuit and U.S.D.C. Northern District of Indiana.

EDITOR'S NOTE

THE FOLLOWING PAGES WERE POOR HARD COPY AT THE TIME OF FILMING. IF AND WHEN A BETTER COPY CAN BE OBTAINED, A NEW FICHE WILL BE ISSUED.

ORIGINAL

96-7185 (2)

No. _____

Supreme Court, U.S.
FILED
DEC 18 1996
OFFICE OF THE CLERK

In The

SUPREME COURT OF THE UNITED STATES

October Term, 1996

GARRIT BATES, *Petitioner*,

v.

UNITED STATES OF AMERICA, *Respondent*,

Petition for Writ of Certiorari
To The United States Court of Appeals
For The Seventh Circuit

PETITION FOR WRIT OF CERTIORARI

Mr. C. Richard Oren
Attorney for Petitioner
1104 Main Street
P.O. Box 532
Rochester, Indiana 46975
(219) 223-9485

41 pp

QUESTION PRESENTED

Must the United States of America prove fraudulent intent on the part of the defendant, Garrit Bates, as an essential element of the crime of knowingly and willfully misapplying federally insured funds, proscribed by 20 U.S.C. §1097(a)?

TABLE OF CONTENTS

Question Presented . . . . . p. i

Table of Contents . . . . . .p. ii

Table of Authorities . . . . . p. iii

Opinions Below . . . . . p. 1

Jurisdiction . . . . . p. 1

Statutory Provision Involved . . . . . p. 2

Statement of the Case . . . . . p. 2

A. Factual Background . . . . . p. 2
B. Procedural History . . . . . p. 3

Reasons for Granting the Petition . . . . . p. 4

I. The Court of Appeals Construction of 20 U.S.C. §1097(a) Conflicts with the Construction of §1097(a) by the Eleventh Circuit Court of Appeals . . . . . p. 5

II. The Question Presented is Important . . . .p. 7

III. The Decision of the Court of Appeals is Erroneous and Confuses the Law in Stating the Working Definition of "Willful Misapplication". . . . . p. 10

Conclusion . . . . . p. 14

Appendix . . . . . .

A. United States v. Bates, No. 95-2203, United States Seventh Circuit Court of Appeals, decided September 20, 1996 . . . .p. A-1

B. United States v. Garret Bates, Cause No. 3: 94-CR-68RM, United States District Court, Northern District of Indiana, South Bend Division: Memorandum and Order rendered April 17, 1995 . . . . . p. A-14

TABLE OF AUTHORITIES

CASES

California Cosmetology Coalition v Riley 871 F. Supp. 1263 . . . . . .p. 12

Dennis v. United States, 341 U.S. 494 (1951) . . .p. 11

Liparota v. United States, 471 U.S. 419 (1985) . .p. 11

Morissette v United States 342 U.S. 246 (1952). .pp. 8,11

United States v Bailie, 99 F. 3d 1147; 1996 WL 580350 . . . . . pp. 6,10, 11

United States v. Jakeway 783 F. Supp. 590 . . . . p. 13

United States v Kammer, 1 F. 3d 1161 (11th Cir., 1993)(Appendix A) . . . . . pp. 4,5,6

United States v Muniz 374 U.S. 150 (1963). . . . .p. 7

United States v. Ranum 96 F. 3d 1020 (7th Cir., 1996) . . . . . p. 11

United States v. Robinson 915 F. 2d 1566; 1990 WL 153988 . . . . . p. 7

United States v Ross, 948 F. 2d 1283; 1991 WL 240481 . . . . . .p. 9

United States v. United States Gypsum, Co., 438 U.S. 422 . . . . . p. 11

United States v. Wolf 820 F. 2d 1499 (9th Cir. 1987) . . . . . .p. 14

STATUTES

18 U.S.C. § 2 . . . . . p. 3

20 U.S.C. §1097(a) . . . . . pp. 2,3,5,6,7, 8,9,10,12,13

28 U.S.C. §1254(1) . . . . . .p. 1

In The

SUPREME COURT OF THE UNITED STATES

October Term, 1996

GARRIT BATES, *Petitioner*,

v.

UNITED STATES OF AMERICA, *Respondent*,

Petition for Writ of Certiorari To The United States Court of Appeals For The Seventh Circuit

Mr. Garrit Bates respectfully petitions for a Writ of Certiorari to review the judgement of the United States Court of Appeals for the Seventh Circuit in this case.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Seventh Circuit (Appendix A, *infra*, pp.A-1 to A-13) is reported at 96 Fed. 3d 964. The opinion of the District Court (Appendix B, *infra*, pp. A-14 to A-23) is unreported.

JURISDICTION

The Court of Appeals entered its judgement on September 20, 1996. The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

STATUTORY PROVISION INVOLVED

20 U.S.C. §1097(a) provided, prior to its amendment in 1992, that:

> Any person who knowingly and willfully embezzles, misapplies, steals, or obtains by fraud, false statement, or forgery any funds, assets, or property provided or insured under the subchapter and part C of subchapter I of Chapter 34 of Title 42 shall be fined not more than $10,000 or imprisoned for not more than Five (5) years, or both; but if the amount so embezzled, misapplied, stolen, or obtained by fraud, false statement, or forgery does not exceed $200, the fine shall not be more than $1,000 and imprisonment shall not exceed One (1) year, or both.

STATEMENT OF THE CASE

A. Factual Background

Mr. Garrit (Jerry) Bates, began employment with Education America, Inc., in January of 1986. Education America, Inc., operated vocational and technical schools located in Indiana and Wisconsin. Mr. Bates held the nominal title of vice-president of Education America, Inc., with his primary responsibility being overseeing student recruitment at various schools. Mr. Bates had no ownership interest in Education America, Inc.

In late 1988 or early 1989, Education America, Inc., realized that Acme Institute of Technology, located in South Bend, Indiana, ("Acme") was experiencing financial difficulty. As a result of this difficulty, Mr. Bates was given the additional responsibility in 1989 of determining which bills of Acme's were to be paid first, in an effort to steer the school

through the financially troubled times. Ultimately, the efforts of Mr. Bates and others involved at Acme and Education America, Inc., were unsuccessful in resuscitating the financial health of the school, with Acme ceasing operations on June 5, 1990. At the time it ceased operations, Acme had unpaid refund liability under the guaranteed student loan program which was substantial.

In January 1991, Mr. Bates began employment with the Indiana Public Employees Retirement Fund where he presently remains employed. Mr. Bates voluntarily cooperated with the investigation of the Department of Education into the refund liability of Acme throughout the calendar year of 1992.

B. Procedural History

Mr. Bates was indicted by a federal grand jury on September 8, 1994. The indictment charged Mr. Bates with knowingly and willfully misapplying specified amounts of federally guaranteed student loan funds on twelve (12) separate occasions between January 15 and June 15, 1990, in violation of 20 U.S.C. §1097(a) and 18 U.S.C. §2. Mr. Bates moved to dismiss the indictment on February 7, 1995. Mr. Bates contended that the indictment did not reveal any alleged facts which would support a conclusion that Mr. Bates had converted any funds guaranteed or furnished by the United States; and, that the indictment failed to allege that Mr. Bates intended to fraudulently convert funds guaranteed or owned by the United States Department of Education.

On April 17, 1995, the United States District Court entered its memorandum and order dismissing the indictment, agreeing with Mr. Bates that the indictment had failed to allege fraudulent intent on the part of Mr. Bates as an essential element of the crime. Specifically, the District Court found that the indictment was insufficient on its face in that each count of the indictment failed to state that Mr. Bates misapplied protected funds "with an intent to injure or defraud the United States."

On May 17, 1995, United States of America filed its notice of appeal. After submission of briefs, the matter was argued on February 12, 1996, before the United States Court of Appeals for the Seventh Circuit. The opinion of the Seventh Circuit was issued on September 20, 1996, reversing the United States District Court by vacating the judgement of the Court dismissing the indictment and reinstating the prosecution. In so doing, the United States Court of Appeals found that the specific intent of a defendant to injure or defraud the United States is not an element of the offense charged.

REASONS FOR GRANTING THE PETITION

The United States Court of Appeals for the Seventh Circuit acknowledged that its opinion in this case conflicts with the Eleventh Circuit Court of Appeals in *United States v Kammer*, 1 F. 3d 1161 (1993). (See, Appendix A, p. A-7) Unpublished opinions issued in at least two (2) other circuit courts of appeal illustrate further conflict, including attempts to

factually distinguish *Kammer*, as well as inconsistency in the government's application of the element of fraudulent intent to the prosecution of alleged acts of misapplication of funds proscribed by §1097(a). At the district court level, indictments involving misapplication of funds in violation of §1097(a) are proliferating and undoubtedly number thousands of defendants nationwide. The need for guidance from this Court is acute. This case is a timely and rare opportunity to provide that guidance since there are systemic reasons why few defendants are ever in a position to present this issue of statutory construction for appellate review. Moreover, the decision below is erroneous and the issue that it addresses is important.

I.

The Court of Appeals Construction of 20 U.S.C. §1097(a) Conflicts with the Construction of §1097(a) by the Eleventh Circuit Court of Appeals.

In *Kammer*, the Eleventh Circuit Court of Appeals faced the identical issue faced by the Seventh Circuit Court of Appeals in the instant case. The Eleventh Circuit held that to prove the crime of misapplication of funds as proscribed by 20 U.S.C. §1097 (a), "... the government must prove (1) a conversion of the property to the use of the defendant or a third party, and (2) fraudulent intent." See, 1 F. 3d 1161, 1165. However, the Seventh Circuit in this case expressly rejected the Eleventh

Circuit's holding, instead concluding

> that intent to injure or defraud the United States is not an element of willful misapplication under §1097(a). Rather, the government must prove that the defendant misapplied-i.e., converted-Title IV funds and that he did so knowingly and willfully.
> (Appendix A, p. A-10).

This issue was also recently addressed by the Ninth Circuit Court of Appeals in an unpublished disposition of the matter of *United States v Bailie*, 99 F. 3d 1147; 1996 WL 580350. In *Bailie*, the Ninth Circuit failed to find an abuse of discretion in the district court's refusal to give a defendant's proposed jury instruction which stated that "an intent to defraud is an intent to deceive or cheat." The Ninth Circuit noted that the defendant had failed to properly place before the court the issue of whether an intent to defraud was an element of the crime of misapplication. However, the Ninth Circuit did find that the district court's instructions to the jury did not misstate the elements of the statutory crime of misapplication of funds under §1097(a) so as to mislead the jury. The Ninth Circuit also indicated that they were not persuaded by the holding of *Kammer* primarily because the government in *Bailie* pursued a different factual theory to establish a misapplication of funds than the factual theory promoted by the government in *Kammer*.

The *Bailie* case illustrates that without guidance from this Court various circuit courts of appeals will be tempted to engage in *ad hoc* formulation of legal principles to justify a particular

court's perspective of the equities of the factual circumstances of a given case.

Further, the Fourth Circuit Court of Appeals has upheld the conviction of a defendant for misapplication of funds in violation of §1097(a) by holding that the evidence supported a jury finding of "the requisite showing of specific intent for conviction of misapplication of student loan funds." See, *United States v. Robinson* 915 F. 2d 1566; 1990 WL 153988. In *Robinson*, the government specifically agreed that specific intent was an element of the crime of misapplication of funds under §1097(a), thus differing from the government's position in this case.

A split of opinion on an important question where two (2) courts of appeal had previously reached contrary results has been found by this Court to be sufficient to grant certiorari. See, *United States v Muniz* 374 U.S. 150, 151 (1963). The foregoing demonstrates such a split of opinion among the circuit courts of appeal; this Court should grant certiorari to review these important conflicts.

II.

The Question Presented is Important.

The question of whether fraudulent intent on the part of a defendant is an essential element of the crime of misapplication of funds as proscribed by 20 U.S.C. §1097(a) is indeed important as it speaks directly to the basic underlying tenet of criminal

culpability, e.g. an evil purpose. Further, in addition to Mr. Bates, there are apparently thousands of defendants who face the possibility of indictment for misapplication of funds in violation of §1097(a), all of whom could be potentially affected by resolution of this issue.

This Court has examined the history of criminal culpability in American jurisprudence and has noted that there has been unanimous adherence to a central thought that " ... wrongdoing must be conscious to be criminal ... ." See, *Morissette v United States* 342 U.S. 246, 252 (1952). This Court further acknowledged that courts of various jurisdictions had utilized such concepts as fraudulent intent and *mens rea* to signify an evil purpose or mental culpability and "... protect those who are not blameworthy in mind from conviction of infamous common law crimes." *Id.* The construction of the crime of misapplication of funds under §1097(a) applied by the Eleventh Circuit would continue this noble tradition of protecting those who are not blameworthy in mind from the harshness of criminal penalty and the stigma of criminal conviction. The construction of §1097(a) urged by the Seventh Circuit, by eliminating the element of fraudulent intent from the crime of misapplication of funds, would erode this tradition of American criminal justice and serve to shift the focus of criminal culpability from the state of mind of an alleged wrongdoer to focus merely on the outcome and result of various acts as the basis for finding criminal culpability. Such an erosion blurs meaningful distinction between negligent

conduct and criminal conduct. For this reason alone, the issue is important.

The issue is also important by virtue of the effect its resolution will have not only upon Mr. Bates but upon actual or potential defendants who are the subject of investigations for misapplication of funds pursuant to §1097(a). An estimate that these actual and potential defendants would number in the thousands is supported by testimony of a government witness in the case of *United States v Ross*, 948 F. 2d 1283; 1991 WL 240481 (4th Cir.,1991). In *Ross* evidence was adduced indicating that at one school in one city approximately One Hundred (100) individuals were investigated for misapplying funds in violation of §1097(a), with over Fifty (50) of those individuals being indicted. Even without the ready availability of precise numbers, a common sense knowledge of the number of institutions of post-secondary education within the Unites States which participate in Department of Education programs offering federally insured funding would surely support an estimate of thousands of potential defendants in any given year across the United States. The magnitude of the application of this criminal statute also renders importance to the issue presented to the court for consideration.

This Court should grant the petition to ensure consistent application of the law to those citizens under investigation for possible violation of §1097(a).

III.

The Decision of the Court of Appeals is Erroneous and Confuses the Law in Stating the Working Definition of "Willful Misapplication".

Mr. Bates contends that the decision of the Seventh Circuit in this case is erroneous and that the working definition of willful misapplication under §1097(a) supplied by the court merely confuses, rather than clarifies the law. The opinion is erroneous in that (1) it eliminates the *mens rea* necessary to elevate the alleged conduct complained of to the level of criminal activity; (2) the opinion contravenes the rule of lenity in statutory construction; (3) the opinion ignores the impact of the 1992 amendment to 20 U.S.C. §1097(a), which specifically criminalized the act of failing to make refunds of unearned student loans. The working definition is also confusing and for that reason could lead to violations of civil regulations forming the basis of criminal convictions.

The Honorable Judge Reinhart of the Ninth Circuit Court of Appeals correctly asserted in his vigorous dissent in *Bailie, supra*, p. 9, that the "... majority wrongly concludes that 20 U.S.C. §1097(a) imposes no intent requirement." In the following passage, Judge Reinhart succinctly demonstrates that to omit a *mens rea* requirement to prove misapplication of funds in violation of §1097(a) is in contravention of existing precedent of this Court:

> The Supreme Court has repeatedly interpreted criminal statutes as having a *mens rea* requirement, absent congressional direction to the contrary. See, e.g., *Liparota v. United States*, 471 U.S. 419, 433-34 (1985). To do otherwise, as the majority does here, would permit a jury to convict a defendant without first finding that the defendant intended to do anything illegal. The Supreme Court, however, has repeatedly declined to construe criminal statutes as imposing strict liability. See, *United States v. United States Gypsum, Co.*, 438 U.S. 422, 436-37 ("[t]he existence of a *mens rea* is the rule of, rather than the exception to, the principles of Anglo-American criminal jurisprudence," *Dennis v. United States*, 341 U.S. 494, 500 (1951)); *Morissette v United States*, 342 U.S. 246, 250 (1952) ("The contention that an injury can amount to a crime only when inflicted by intention is no provincial or transient notion. It is as universal and persistent in mature systems of law as belief in freedom of the human will and a consequent ability and duty of the normal individual to choose between good and evil.").
>
> *Bailie*, p. 9

The holding of the Seventh Circuit in this case is also in contravention of this Court's precedent of applying the rule of lenity in statutory construction. Although the Seventh Circuit, in 1996 acknowledged that " ... ambiguity concerning the meaning of statutory language 'should be resolved in favor of lenity,' ... " (see, *United States v. Ranum* 96 F. 3d 1020, 1030), the Seventh Circuit did not apply the rule of lenity in this case. In failing to apply the rule of lenity, the Seventh Circuit ignored the precedential value of Justice Brennan's statement that "... requiring *mens rea* is in keeping with our long standing recognition of the principle that 'ambiguity concerning the ambit of criminal statute should be resolved in favor of lenity' ...". *Liparota, supra* 427.

Although "... the rule of lenity is not to be applied where to do so would conflict with the implied or expressed intent of Congress ..." (*Id*, p. 427), the legislative history of §1097(a) indicates that Congress has acknowledged the existence of a *mens rea* requirement in the crime of misapplication of funds. As has been recognized by at least one (1) United States District Court, in 1992 Congress amended §1097(a) to include "... provisions criminalizing the failure to refund funds, assets, or property provided or insured under the Title IV programs." See, *California Cosmetology Coalition v Riley* 871 F.Supp. 1263, 1265. Prior to the 1992 amendments, the failure to refund Title IV funds were necessarily prosecuted, as in this case, as a misapplication of funds under §1097(a). The 1992 amendment of §1097(a) by Congress imposes strict criminal liability for failing to make refunds.[1] This indicates Congress' tacit acknowledgement that the crime of misapplication of funds does not impose strict criminal liability, for had it so done the 1992 amendment would have been unnecessary. Instead, a greater burden of proof is imposed upon the prosecution; that being proof of the particular conduct complained of and evidence of *mens rea*.

---

1. 20 U.S.C. §1097(a), after its amendment in 1992, reads:
Any person who knowingly and wilfully embezzles, misapplies, steals, obtains by fraud, false statement or forgery, or fails to refund any funds, assets or property provided or insured under this subchapter and part C of subchapter I of chapter 34 of Title 42 or attempts to so embezzle, misapply, steal, obtain by fraud, false statement or forgery or fail to refund any funds, assets or property shall be fined not more than $20,000.00 or imprisoned for not more than 5 years, or both except if the amount so embezzled, misapplied, stolen, obtained by fraud, false statement, or forgery, or failed to be refunded does not exceed $200.00, then the fine shall not be more than $5,000.00 and imprisonment shall not exceed 1 year, or both.

Finally, the Seventh Circuit opinion in this case should not stand because the "working definition" of willful misapplication under §1097(a) which is provided is so confusing that the simple violation of a civil regulation could result in a conviction for criminal conduct. The working definition of the Seventh Circuit in this case

> requires the government to allege and prove that the defendant consciously, voluntarily, and intentionally exercised unauthorized control or dominion over federally provided or guaranteed Title IV funds that interfered with the rights of the funds true owner(s), for the use and benefit of the defendant or a third person, while knowing that such an exercise of control or dominion over the funds was a violation of the law. (See, Appendix A, p. A-11)

The first part of the working definition essentially states the crime of conversion. See, *United States v. Jakeway* 783 F. Supp. 590, 597. The working definition then further requires that the criminal conversion be committed with the knowledge that the criminal conversion was a "violation of the law." This final element in the Seventh Circuit's working definition truly begs the question - - -, what law must the defendant know he is violating?

An attempt to apply this working definition to the facts of any case would be fraught with a risk that a jury would consider a knowing violation of a civil regulation as sufficient to impose criminal liability. This type of conclusion would be erroneous and lead to unjust results, for even though violation of a civil regulation may be used to establish motive or intent,

violation of a civil regulation is not admissible where it is used to supply a crucial element of the government's case. See, *United States v. Wolf* 820 Fed 2d 1499, 1504-05 (9th Cir. 1987); *cert. denied* 45 U.S. 960 (1988).

It is quite conceivable that the working definition would allow the jury to look to the violation of a single civil regulation to supply both the "unauthorized" component of "the exercise of dominion or control", and the finding that the criminal conversion was a knowing violation of the law. This thinking would inevitably result in a knowing violation of a civil regulation being punished as criminal conduct. The working definition supplied by the Seventh Circuit is, in effect, so confusing that it is unworkable and unjust.

This Court should grant Mr. Bates' petition to resolve the conflict among the circuits and correct the Seventh Circuit's error.

CONCLUSION

The Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

C. Richard Oren, ISBA #15074-25
1104 Main Street
P.O. Box 532
Rochester, Indiana 46975
(219) 223-9485
ATTORNEY FOR PETITIONER

APPENDIX A

In the

United States Court of Appeals

For the Seventh Circuit

No. 95-2203
UNITED STATES OF AMERICA,
Plaintiff-Appellant,

v.

GARRIT BATES,
Defendant-Appellee.

Appeal from the United States District Court
for the Northern District of Indiana, South Bend Division.
No. 94 CR 68—Robert L. Miller, Jr., *Judge.*

ARGUED FEBRUARY 12, 1996—DECIDED SEPTEMBER 20, 1996

Before CUDAHY, FLAUM, and KANNE, *Circuit Judges.*

KANNE, *Circuit Judge.* After Garrit Bates was charged with twelve counts of willfully misapplying federally guaranteed Title IV student aid funds, he filed a pretrial motion to dismiss the indictment as insufficient. Specifically, he argued that both conversion and intent to injure or defraud the federal government are elements of the offense of willfully misapplying financial aid monies and that the indictment had failed to adequately allege either one. The district court granted his motion to dismiss after determining that the indictment failed to allege intent to injure or defraud the United States, and the government appeals to this court. Because we find that a conviction

for willful misapplication of Title IV funds does not require proof of the defendant's intent to injure or defraud the United States, and that the indictment is otherwise sufficient, we vacate the judgment of the district court and reinstate the prosecution.

I. History

Given that the district court determined that the indictment was insufficient on its face, for this appeal we take the facts as they are alleged in the indictment, which are set out below. James and Laurenda Jackson are the owners and operators of Education America, Inc., a for-profit consulting and management firm for various technical and vocational schools. In December 1986, the Jacksons acquired ownership of the Acme Institute of Technology, a not-for-profit technical school located in South Bend, Indiana. After the acquisition, the Jacksons appointed Bates, who was vice president of Education America at the time, to act as Acme's chief financial officer and treasurer of the Acme board of trustees.

On April 30, 1987, Mr. Jackson, acting as president of Acme, signed a program participation agreement with the Department of Education. Under the agreement, Acme became authorized to receive student loan checks through the Title IV federal Guaranteed Student Loan ("GSL") program, but participation in the program was contingent upon (1) Acme's continued accreditation by an approved accrediting association, and (2) Jackson's promise to comply with all statutes and regulations governing the GSL program. Around the same time, Bates signed a similar participation agreement for a different school owned by Education America, and he therefore presumably understood the responsibilities imposed by the Acme participation agreement.

Through the GSL program, banks and other private financial institutions would lend money to Acme students for tuition and other educational expenses. The federal government's role was to administer the loan program and

guarantee payment of the loans in the event any of the student borrowers defaulted. Loan checks were mailed directly to Acme and, once endorsed, were credited against the student's tuition debt. However, if a student with a GSL withdrew from Acme prior to completion of a term, federal regulations required Acme to refund a portion of the loan proceeds to the lender within 30 or 60 days from withdrawal (depending on the date of the loan application), which was then to be deducted from the amount owed. Of course, if loan refunds were not made, the student—and, in the event of default, the government—would nonetheless remain liable to the lender for the full amount of the loan.

On April 14, 1988, Mr. Jackson sent a letter to the director of Acme instructing him (1) to remit 10 percent of Acme's gross receipts from the previous month to Education America as a management fee, and (2) to arrange for a specified monthly salary to be paid by Acme to the Jacksons. The letter explained that if these required payments caused Acme to experience a cash shortfall, Education America would loan money back to Acme in order to cover the discrepancy. As chief financial officer of Acme, Bates had the authority to determine which of Acme's bills would be paid as they came due, and he repeatedly gave these fee and salary payments to Education America and the Jacksons priority over refunds to lenders of student loan monies for withdrawn students. In doing this, Bates would specifically direct Acme employees not to make required student loan refunds. By the end of September 1988, Acme had amassed a GSL refund debt of approximately $55,000.

In late 1988 or very early 1989, Education America officials directed Acme to discontinue using a special bank account that was designed to segregate unearned student loan monies (those that should have been earmarked for refunds) from the school's general funds account. When Acme's refund arrearage had grown to around $68,000 by January 1989, Acme's financial aid director sent a letter to Mr. Jackson frustratedly pointing out the seriousness

of failing to pay refunds of Title IV monies. In March 1989, Acme's unpaid student loan refunds totaled $85,000. That month, Bates notified Acme's financial aid director, at her request, that she was absolved of all legal responsibility concerning refunds on GSLs and that such refunds would be "solely the responsibility and decision of the corporate office."

In April 1989, the National Association of Trade and Technical Schools ("NATTS"), a national accrediting association, performed an on-site audit of Acme for the purpose of determining whether it should continue to accredit the school. In its May 1990 report to the Department of Education, NATTS found that Acme had "inadequately demonstrated its ability to make appropriate and timely refunds," and that it had "loaned substantial amounts of money" and engaged in the "upstreaming" of management fees to Education America and its owner, Mr. Jackson, who also happened to be Acme's president and chairman of the board of trustees.

After losing its accreditation, Acme received notice from the Department of Education that effective March 8, 1990, Acme was no longer eligible to participate in the GSL program. On June 5, 1990, Acme closed its doors, having accrued a total student loan refund debt of $139,649, not including interest and certain special allowances.

On September 8, 1994, a federal grand jury handed down a twelve-count indictment against Bates. Following a recitation of the facts set out above, the indictment charges that on twelve separate occasions between January 15 and June 15, 1990, Bates knowingly and willfully misapplied specified amounts of federally guaranteed student loan funds, in violation of 20 U.S.C. § 1097 and 18 U.S.C. § 2. At the time of Bates's alleged wrongdoing in 1990, § 1097(a) declared guilty of a crime "[a]ny person who knowingly and willfully embezzles, misapplies, steals, or obtains by fraud, false statement, or forgery any funds, assets, or property provided or insured under [Title IV of the Higher Education Act of 1965] . . . ." 20 U.S.C. § 1097(a).

On February 7, 1995, Bates filed a motion to dismiss the indictment. The memorandum in support of his motion argued first that conviction under § 1097(a) for willful misapplication of student aid funds requires proof of both conversion and the defendant's intent to injure or defraud the United States, and second, that the indictment failed to allege sufficient facts to constitute conversion and neglected to allege intent to injure or defraud the United States at all. The district court agreed that § 1097(a) requires proof of the intent to injure or defraud the government and that the indictment had failed to allege such intent, and it therefore granted the motion and dismissed the indictment.

II. Analysis

The government appeals from the judgment of dismissal, arguing (1) that a conviction for willful misapplication of Title IV funds does not require that the government demonstrate the defendant's intent to injure or defraud the United States, and (2) that regardless of whether § 1097(a) requires a showing of such intent, the indictment was facially sufficient. We address these separate arguments in turn. Our review of a district court's determination concerning the facial sufficiency of an indictment is *de novo*. *Frank v. United States*, 914 F.2d 828, 830 (7th Cir. 1990) (citing *United States v. Bucey*, 876 F.2d 1297, 1301-02 (7th Cir.), *cert. denied*, 493 U.S. 1004 (1989)). We likewise engage in plenary review of a district court's statutory interpretation. *United States v. Shriver*, 980 F.2d 456, 459 (7th Cir. 1992).

A. Intent to Injure or Defraud the United States

A basic tenet of criminal law provides that *actus non facit reum nisi mens sit rea*, meaning an act does not make one guilty unless his mind is guilty. Thus, at common law, nearly all crimes required proof that the defendant not only committed a wrongful act, but that he did so with the requisite *mens rea*, or culpable mental state.

As history has witnessed the statutory codification of criminal offenses, enacting legislatures have employed such words as "intentionally," "willfully," or "purposefully" to signify the common law requirement of mental culpability. *See Morissette v. United States*, 342 U.S. 246, 251-52, 72 S. Ct. 240, 244 (1952).

But criminal intent (even when differentiated from such other, lesser mental states as objective knowledge, recklessness, or negligence) is an elusive concept—some crimes may demand proof of only the defendant's *general* intent to engage consciously and voluntarily in the proscribed conduct, while other crimes may additionally require proof of the defendant's *specific* intent to effectuate a particular result. 1 WAYNE R. LAFAVE & AUSTIN W. SCOTT, JR., SUBSTANTIVE CRIMINAL LAW § 3.5, at 302-18 (1986 & Supp. 1996). On this appeal, we must reach the question we declined to answer in *United States v. Ross*, 77 F.3d 1525, 1546 (7th Cir. 1996): whether conviction under 20 U.S.C. § 1097(a) for willfully misapplying federally insured student aid funds requires the government to allege and prove the defendant's specific intent to injure or defraud the United States.

In *Morissette*, the Supreme Court instructed:

> [W]here Congress borrows terms of art in which are accumulated the legal tradition and meaning of centuries of practice, it presumably knows and adopts the cluster of ideas that were attached to each borrowed word in the body of learning from which it was taken and the meaning its use will convey to the judicial mind unless otherwise instructed.

342 U.S. at 263, 72 S. Ct. at 250. Congress has utilized the expression "willful misapplication" in a host of criminal statutory provisions. And thus, although few of these crimes are (as in *Morissette*) centuries old, we have much to which we may turn by way of analogy in discerning the elements of willful misapplication, as the term is used in § 1097(a).

Bates contends, citing *United States v. Kammer*, 1 F.3d 1161, 1165 (11th Cir. 1993),* and *United States v. Jakeway*, 783 F. Supp. 590, 597 (M.D. Fla. 1992), that we should look for guidance to our interpretation of 18 U.S.C. § 656, which prohibits bank insiders from, among other things, willfully misapplying the bank's funds. This court, like the Eleventh and most of our other sister circuits, has defined the crime of willfully misapplying bank funds to require proof (1) that the defendant intentionally converted bank funds to his own use or the use of another, and (2) that the defendant did so with the specific intent to injure or defraud the bank. *United States v. Crabtree*, 979 F.2d 1261, 1266-67 (7th Cir. 1992), *cert. denied*, 510 U.S. 878 (1993); *United States v. Bruun*, 809 F.2d 397, 408 (7th Cir. 1987). Either the intent to injure *or* the intent to defraud will suffice, and they are not the same. *United States v. Bates*, 852 F.2d 212, 215 (7th Cir. 1988); *United States v. Angelos*, 763 F.2d 859, 861 (7th Cir. 1985). For the defendant to have acted with the intent to injure the bank, "it is sufficient that the loan officer engaged in acts, the natural tendency of which would be to injure the bank." *Crabtree*, 979 F.2d at 1268 (quoting *Bruun*, 809 F.2d at 408). Intent to defraud the bank, on the other hand, "means to take financial advantage of a confidential relationship and does not require any intent to injure the bank." *Bates*, 852 F.2d at 215-16 (citing *Angelos*, 763 F.2d at 861-62).

The government concedes that willful misapplication of federally guaranteed student aid funds requires the defendant to have intentionally converted such funds to his own use or the use of a third party, but it argues that the defendant's specific intent to injure or defraud the United States is not an element of the offense. We agree.

---

* Because this opinion conflicts with the Eleventh Circuit's holding in *Kammer*, it was circulated before release to all judges in active service pursuant to 7th Cir. R. 40(e). No judge requested a rehearing en banc.

The mere fact that we have interpreted willful misapplication of bank funds to require both intentional conversion *and* the intent to injure or defraud the bank does not necessitate the conclusion that specific fraudulent or injurious intent is part and parcel of "willful misapplication." In fact, quite the opposite is true. Intent to injure or defraud the bank is not subsumed within the phrase "willful misapplication," but rather is a separate and distinct component of § 656. *See Crabtree*, 979 F.2d at 1266 (noting that § 656 requires both "that the defendant willfully misapplied funds of the bank" and that he did so "with the intent to injure or defraud the bank"). The point is further illustrated by the Fifth Circuit's recent approval of the following instructions in a bank fund misapplication case:

> To willfully misapply a bank's money or property means an intentional conversion of such money or property to one's own use and benefit, or for the use and benefit of another, knowing that one had no right to do so.
>
> To act with the intent to defraud means to act with an intent to deceive or cheat someone, ordinarily for the purpose of causing some financ[ial] loss to another or bringing about some financial gain to oneself.

United States v. Giraldi, No. 94-60602, 1996 WL 339177, at *8 (5th Cir. June 19, 1996). Thus, intent to injure or defraud is an offense element that must be proved *in addition to* willful misapplication in a § 656 prosecution.

It is true that the language of § 656, like that of § 1097(a), does not explicitly require the defendant to have acted with specific fraudulent or injurious intent. However, there is a historical rationale for reading into § 656 the requirement of the defendant's intent to injure or defraud the bank. In *Bates*, we explained:

> The current statutory language does not expressly require any proof of [fraudulent or injurious] intent. Originally the statute did require proof of intent to "injure or defraud" the bank or "deceive" a bank officer but these words were inadvertently dropped in the course of a technical revision of the criminal code. To avoid making every unauthorized loan by a bank officer a willful misapplication of bank funds, courts, including our own, read the missing words back into the section.

852 F.2d at 215 (citing *Angelos*, 763 F.2d at 861; *United States v. Shively*, 715 F.2d 260, 266 (7th Cir. 1983), *cert. denied*, 465 U.S. 1007 (1984)). Section 1097(a) has never included a requirement that the defendant have acted with an intent to injure or defraud the government, and with no textual or historical basis for doing so, we are reluctant to read such a requirement into the statute.

Our reluctance is bolstered by this circuit's prior analysis of 18 U.S.C. § 665, another statute prohibiting the willful misapplication of federal funds—specifically, Comprehensive Employment and Training Act ("CETA") funds. In *United States v. Hamilton*, a defendant charged under § 665 with willful misapplication of CETA funds argued that he could not be convicted because he did not know the monies he misapplied were federal funds. 726 F.2d 317, 320 (7th Cir. 1984). Under § 656, a defendant cannot be convicted if he did not know the funds were the bank's because he must have acted with intent to injure or defraud the bank, and thus Hamilton urged this court to pattern our interpretation of § 665's requirements after those of § 656. *Id.* We refused to employ such an analogy, explaining that "we need not wander that far afield, since a closer analogy is found in the general section concerning embezzlement of public money, 18 U.S.C. § 641." *Id.* (citing *United States v. Coleman*, 590 F.2d 228 (7th Cir. 1978), *cert. denied*, 440 U.S. 980 (1979)).

Section 641, as construed in *Morissette*, requires only that the defendant intentionally converted public funds to his own use and benefit or to that of a third person. 342 U.S. at 263, 270-72, 72 S. Ct. at 250, 254. Thus, in *United States v. Brown*, we held that " 'misapplication of funds' for purposes of § 665 mean[s] the conversion of funds to

the defendant's own use or the use of another," and that "the conversion of CETA funds for the use of uncertified workers when the defendant knows of their uncertified status is a willful misapplication of funds for purposes of § 665." 742 F.2d 363, 366-67 (7th Cir. 1984). *But see United States v. Garcia*, 751 F.2d 1033, 1037 (9th Cir. 1985) (holding that intent to injure or defraud the United States is an essential element of willful misapplication under § 665). In *Hamilton*, we declined to read into § 665 a § 656-esque requirement that the defendant have acted with intent to injure or defraud the United States, holding:

> We believe that Congress, through § 665, desired to afford federal protection to the large sums of federal money entrusted to nonfederal agencies to accomplish the purposes of CETA, and did not intend to limit this protection to situations where the defendant was aware of a federal interest in the funds.

726 F.2d at 320. This reasoning applies equally here, where Congress has sought through § 1097(a) to provide broad protection for Title IV student financial aid funds entrusted to private educational institutions.

We conclude, therefore, that intent to injure or defraud the United States is not an element of willful misapplication under § 1097(a). Rather, the government must prove that the defendant misapplied—i.e., converted—Title IV funds and that he did so knowingly and willfully. The Supreme Court has defined willfulness as the "voluntary, intentional violation of a known legal duty." *United States v. Pomponio*, 429 U.S. 10, 12-13, 97 S. Ct. 22, 24 (1976). Conversion is an "unprivileged interference with the owner's possession and enjoyment of a chattel." *Kerrigan v. American Orthodontics Corp.*, 960 F.2d 43, 45 (7th Cir. 1992); *see also Ross*, 77 F.3d at 1546 (quoting *Kammer*'s definition of conversion as "an act of dominion or control over the property that seriously interferes with the owner's rights," 1 F.3d at 1165). *Morissette* explained:

> Conversion . . . may be consummated without any intent to keep and without any wrongful taking, where the initial possession by the converter was entirely lawful. Conversion may include misuse or abuse of property. It may reach use in an unauthorized manner or to an unauthorized extent of property placed in one's custody for limited use. Money rightfully taken into one's custody may be converted without any intent to keep or embezzle it merely by commingling it with the custodian's own, if he was under a duty to keep it separate and intact.

342 U.S. at 271-72, 72 S. Ct. at 254. Thus, as a working definition, willful misapplication under § 1097(a) requires the government to allege and prove that the defendant consciously, voluntarily, and intentionally exercised unauthorized control or dominion over federally provided or guaranteed Title IV funds that interfered with the rights of the funds' true owner(s), for the use and benefit of the defendant or a third person, while knowing that such an exercise of control or dominion over the funds was a violation of the law.

B. Sufficiency of the Indictment's Allegation of Conversion

In his motion to dismiss, reiterated on appeal, Bates argued that the indictment was insufficient first because it did not allege intent to injure or defraud the government, and second because it failed to allege sufficient facts to constitute conversion. Having decided that intent to injure or defraud is not an element of § 1097(a), this leaves only Bates's argument that the indictment failed to adequately charge conversion.

Facial sufficiency is not a high hurdle. Indictments need not exhaustively describe the facts surrounding a crime's commission nor provide lengthy explanations of the elements of the offense. FED. R. CRIM. P. 7(c)(1) instructs that "[t]he indictment or the information shall be a plain, concise and definite written statement of the essential

facts constituting the offense charged." We have held that "[a]n indictment is sufficient if it: (1) states all the elements of the offense charged; (2) informs the defendant of the nature of the charge, enabling the defendant to prepare a defense; and (3) enables the defendant to plead the judgment as a bar to later prosecution for the same offense." *U.S. v. F.J. Vollmer & Co., Inc.*, 1 F.3d 1511, 1518 (7th Cir. 1993) (citing *United States v. James*, 923 F.2d 1261, 1265 (7th Cir. 1991)), *cert. denied*, 114 S. Ct. 688 (1994). "Generally, an indictment is sufficient when it sets forth the offense in the words of the statute itself, as long as those words expressly set forth all the elements necessary to constitute the offense intended to be punished." *United States v. Hinkle*, 637 F.2d 1154, 1157 (7th Cir. 1981).

Bates argues that the indictment fails to adequately set forth the elements of conversion because it does not charge that his handling of federally guaranteed funds was in any way "unauthorized." Yet, the indictment alleges (1) that the school had a duty to refund unearned student loans to the lender within thirty to sixty days; (2) that due to the participation agreement and the warnings of Acme's financial aid director, Bates knew of this duty; (3) that Bates specifically directed Acme personnel not to make refunds that were required by law; and (4) that Bates instead made management and salary payments to the Jacksons and to Education America, of which Bates happened to be vice president. These factual allegations clearly make out a charge that Bates's handling of Acme's federally guaranteed student loan funds was unauthorized.

Bates also contends, citing *Hinkle*, 637 F.2d at 1158, that the indictment is insufficient because the term "misapplication" is intrinsically vague. In *Hinkle*, we determined that an indictment charging use of a communication device to facilitate the commission of a felony involving a controlled substance, in violation of 21 U.S.C. § 843(b), was insufficient to inform the defendant of the nature of her alleged crimes. *Id.* Bates argues that "misapplication" is as uninformative as "facilitation." But Bates misunderstands the holding in *Hinkle*. The fatal ambiguity in *Hinkle* was that the indictment, although following the language of the statute in alleging the offense of facilitating a felony involving a controlled substance, failed to identify either the felony facilitated or the controlled substance involved. *Id.* The "facilitation" charge was duplicitous because it could have referred to any one of a number of criminal acts that the defendant may have committed.

Here, on the other hand, Bates has been charged with a distinct, identifiable offense: he willfully misapplied specified amounts of federally guaranteed Title IV funds on twelve specified occasions. Although admittedly bareboned, the indictment in this case included all of the requisite elements of willful misapplication under § 1097(a), and it certainly alleged sufficient facts to apprise Bates of the charges against him.

The judgment of the district court dismissing the indictment is VACATED, and the cause is REMANDED to the district court for further proceedings consistent with this opinion.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit

USCA AO7XXXC-92-001—Midwest Law Printing Co., Inc., Chicago—9-20-96

APPENDIX B

UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF INDIANA

SOUTH BEND DIVISION

UNITED STATES OF AMERICA	)	
	)	
vs.	)	CAUSE NO. 3: 94-CR-68RM
	)	
GARRIT BATES	)	

MEMORANDUM AND ORDER

Defendant Garrit Bates' moves to dismiss the indictment against him and for oral argument. Because the parties have adequately briefed the motion to dismiss, the court denies the motion for oral argument. For the following reasons, the court grants the motion to dismiss.

Mr. Bates was indicted on September 8, 1994 on twelve counts of aiding and abetting the knowing and willful misapplication of federally insured funds pursuant to 20 U.S.C. § 1097(a), 18 U.S.C. § 2. Mr. Bates contends that the facts alleged in the indictment could not support a finding that the essential elements of § 1097(a) have been met. The government disagrees both with Mr. Bates's version of the essential elements and with his conclusion that the indictment fails to allege facts that could satisfy those essential elements.

The indictment charges that Mr. Bates was the Treasurer of the Board of Trustees of the Acme Institute of Technology, a not-for-profit technical school owned by James and Laurenda Jackson. Mr. Bates also was Vice-President of Education America,

Inc., which the Jacksons also owned.

Acme students were eligible for guaranteed student loans ("GSLs") under a program enacted by Congress and administered by the Department of Education. If a student withdrew from Acme before a term's completion, federal regulations required Acme to refund a portion of loan proceeds to the lending institution. Federal regulations required that the refunds be paid within 30 or 60 days of the student's withdrawal.

The indictment charges that beginning in 1987, decisions made by the Jacksons and Mr. Bates resulted in Acme beginning a practice of not making refunds on GSLs. In late 1988 or 1989, Education America officials directed Acme to discontinue the use of a special bank account that segregated the refunds from the general account. Around January 1989, according to the indictment, Mr. Bates determined on a week-to-week, or sometimes day-to-day, basis which bills would or would not be paid with the understanding that payments to the Jacksons took precedence over payment of refunds. The indictment alleges that Mr. Bates specifically instructed Acme employees not to make student loan refunds.

On March 13, 1989, Mr. Bates, as Executive Vice-President of Education America, allegedly notified the Financial Aid Director that, pursuant to her request, she was released from all responsibility concerning refunds on GSLs. The letter stated that the refund of any unearned tuition was "solely the responsibility and decision of the corporate office." The Financial Aid Director allegedly was directed, however, to continue to prepare refund

documents to be approved by the corporation for payment.

Effective March 8, 1990, Acme no longer was eligible to participate in the GSL program because Acme had lost its accreditation from the National Association of Trade and Technical Schools. On June 5, 1990, Acme ceased operation and closed its doors; at that time, the amount of unrefunded GSL funds allegedly had accrued to a total of $139,649.00 while Mr. Bates was chief financial officer at Acme.

The indictment then charges, in twelve different counts, that on January 15, January 16, January 29, April 2, twice on April 27, May 7, May 11, May 18, June 9, June 12 and June 15 of 1990, Mr. Bates knowingly and willfully misapplied funds provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code in violation of 20 U.S.C. § 1097(a) and 18 U.S.C. § 2.

The indictment charges Mr. Bates with crimes occurring in 1990. At that time, 20 U.S.C. § 1097(a) defined criminal conduct as follows: "Any person who knowingly and willfully embezzles, misapplies, steals, obtains by fraud, false statement or forgery any funds . . . provided or insured under this subchapter . . . ."

Mr. Bates relies upon United States v. Kammer, 1 F.3d 1161, 1165 (11th Cir. 1993), to argue that, with respect to a charge under § 1097(a), "[t]o establish a criminal misapplication, the government must prove (1) a conversion of the property to the use of the defendant or a third party, and (2) fraudulent intent." United States v. Kammer, 1 F.3d at 1165. Mr. Bates contends that the indictment does not allege facts supporting these essential

elements.

The government responds that the Kammer court's interpretation of the essential elements of § 1097(a) is erroneous. The government contends that the elements necessary to prove the charge of misapplication of funds under § 1097(a) are: (1) that the funds described in the indictment were provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code at the time alleged; (2) that the defendant misapplied such funds; and (3) that he did so knowingly and willfully. The government defines "misapplication" to mean a conversion of funds to the defendant's own use or the use of another.

The government's version of the essential elements restates the elements as they are stated in § 1097(a), but the controversy between Mr. Bates and the government lies in the definition of misapplication of funds. Both parties argue, and the court agrees, that a misapplication requires a conversion, but the parties dispute whether a misapplication under § 1097(a) also requires fraudulent intent.

The government contends that the Seventh Circuit does not always require an intent to defraud with respect to statutes that forbid "misapplication of funds," citing United States v. Brown, 742 F.2d 363 (7th Cir. 1984). Applying 18 U.S.C. § 665 of the Comprehensive Employment and Training Act ("CETA"), the Brown court stated that:

> In United States v. Tamargo, 637 F.2d 346[, 350] (5th Cir.), cert. denied, 454 U.S. 824 (1981), the court approved the trial court's use of a jury instruction that stated that "misapplication of funds" for purposes of §

> 665 meant the conversion of funds to the defendant's own use or the use of another.

742 F.2d at 366. The Brown court said no more regarding the term's definition. The Brown court, however, omitted a critical clause from Tamargo's definition of misapplication of funds, for Tamargo actually states that, "The trial court here properly charged the jury to "misapply money or property means a willful conversion or taking of such money or property to one's own use and benefit or the use and benefit for another, with intent to defraud." United States v. Tamargo, 637 F.2d at 350 (emphasis added). Accordingly, the quoted language from the Brown case has little influence.

Nevertheless, the court is hesitant to follow the Kammer case. The essential elements stated in the Kammer case were derived from United States v. Jakeway, 783 F. Supp. 590, 597 (M.D. Fla. 1992), in which the court explained that although the Eleventh Circuit had not defined "misapplication" in the context of § 1097(a), the term had been defined in the context of 18 U.S.C. § 656, which deals with misapplication of funds by a bank officer or employee. United States v. Jakeway, 783 F. Supp. at 597, n. 6. Thus, the Jakeway court extrapolated the elements of criminal misapplication from United States v. Acosta, 748 F.2d 577, 580 (11th Cir. 1984), which held that misapplication under 18 U.S.C. § 656 is the "willful taking of an insured bank's money by its employee with intent to defraud the bank." United States v. Acosta, 748 F.2d at 580. Therefore, the Kammer holding is founded upon an earlier holding that, under a different statute,

misapplication required fraudulent intent.

The Seventh Circuit has not defined "misapplication" with respect to § 1097(a), but, like the Eleventh Circuit, requires a finding of intent to defraud or injure with respect to misapplication of bank funds under 18 U.S.C. § 656. United States v. Crabtree, 979 F.2d 1261, 1266 (7th Cir. 1992), cert. denied, 114 S. Ct. 217 (1993) (to prove a violation of 18 U.S.C. § 656, the government must prove, among other things, that the defendant willfully misapplied funds of the bank with the intent to injure or defraud the bank).

This does not necessarily compel a conclusion that § 1097(a) also requires fraudulent intent. The fraudulent intent element required under 18 U.S.C. § 656 has a historical basis in the statute itself:

> The current statutory language does not expressly require any proof of intent. Originally the statute did require proof of intent to "injure or defraud" the bank or "deceive" a bank officer but these words were inadvertently dropped in the course of a technical revision of the criminal code. To avoid making every unauthorized loan by a bank officer a willful misapplication of bank funds, courts, including our own, read the missing words back into the statute.

United States v. Bates, 852 F.2d 212, 215 (7th Cir. 1988); see also United States v. Angelos, 763 F.2d 859, 861 (7th Cir. 1985); United States v. Shively, 715 F.2d 260, 266 (7th Cir. 1983), cert. denied, 465 U.S. 1007 (1984) ("these words were dropped by a reviser without intent to alter the meaning of the law").

In United States v. Garcia, 751 F.2d 1033 (9th Cir. 1985), however, the Ninth Circuit affirmed the dismissal of an

indictment for "wilfully misappl[ying]" CETA funds in violation of 18 U.S.C. § 665 because the government conceded it could not prove intent to injure or defraud. United States v. Garcia, 751 F.2d at 1034. In concluding that § 665 requires a specific intent to injure or defraud, the district court had relied on the Ninth Circuit's interpretation of the bank fraud statute, 18 U.S.C. § 656. Id. at 1036. On appeal, the government contended that the analogy between § 656 and § 665 was not compelling because, as discussed above, the original version of § 656 expressly required an intent to injure and defraud the bank, and Congress had expressly disclaimed any intention of changing the law. Id. The Ninth Circuit rejected this contention, stating:

> But this circumstance cuts against the government's reading of the statute. The only reason Congress could have considered the explicit requirement of a purpose to injure or defraud redundant was that Congress understood the term "willful misapplication" to include such an intent by implication.

Id.

Thus, the Ninth Circuit held that a "willful misapplication" for the purposes of § 665 necessarily includes an intent to defraud or injure. In doing so, the court reasoned that:

> In a criminal statute, "willfully" generally means a voluntary, intentional violation of a known legal duty in bad faith or with evil purpose. See United States v. Pomponio, 429 U.S. 10, 11-12 (1976) (per curiam); United States v. Bishop, 412 U.S. 346, 260 (1973). A general intent to commit the proscribed act is not enough; a specific intent to do something the law forbids is required. See United States v. Wilson, 631 F.2d 118, 119 (9th Cir. 1980). The definition of "misapplication" suggests a similar element: "[i]mproper, illegal, wrongful, or corrupt use [or] application of funds, property, etc." Black's Law Dictionary 901 (5th Ed. 1979).

Id. at 1035; see also Morissette v. United States, 342 U.S. 246, 276 (1952) (holding that "knowingly converts" under 18 U.S.C. § 641 required an intention "wrongfully to deprive another of possession of property.").

The Ninth Circuit gave much importance to the fact that the term "willfully misapply" in 18 U.S.C. § 665(a) "is embedded in a series of words referring to harmful or wrongful acts clearly causing financial injury to the United States or impeding the achievement of CETA's goals. All the acts prohibited by the statute are more serious in character than simple violations of procedural requirements." United States v. Garcia, 751 F.2d at 1035-36; see also United States v. Hammen, 977 F.2d 379, 384 (7th Cir. 1992) (in a 18 U.S.C. § 656 case, "[t]he intent to defraud or injure the bank is what separates criminal misapplication from mere maladministration."); United States v. Bates, 852 F.2d at 215 (stating that courts read the intent to defraud or injure back into 18 U.S.C. § 656 "[t]o avoid making every unauthorized loan by a bank officer a willful misapplication of bank funds.").

Similarly, the term "misapply" in § 1097(a) "is embedded in a series of words referring to harmful or wrongful acts clearly causing financial injury to the United States . . ." United States v. Garcia, 751 F.2d at 1035. Further, as was the case in Garcia under 18 U.S.C. § 665, "[a]ll the acts prohibited by [§ 1097(a)] are more serious in character than simple violations of procedural requirements." United States v. Garcia, 751 F.2d at 1036.

The court finds the reasoning of Garcia persuasive, and

thus elects to follow the course of United States v. Kammer, 1 F.3d 1161 in holding that, with respect to a charge under § 1097(a), "[t]o establish a criminal misapplication, the government must prove (1) a conversion of the property to the use of the defendant or a third party, and (2) fraudulent intent." United States v. Kammer, 1 F.3d at 1165. Thus, the essential elements of a willful and knowing misapplication under § 1097(a) include: (1) that the funds described in the indictment were provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code at the time alleged; (2) that the defendant willfully and knowingly misapplied such funds; and (3) that he did so with an intent to injure or defraud the United States. A defendant misapplies funds by converting them to the defendant's own use or the use of another.

Mr. Bates contends that the indictment is defective because it does not allege facts supporting a finding that the defendant's actions constitute violations of § 1097(a). He contends that the indictment fails to recite all of the essential elements of a willful and knowing misapplication under § 1097(a). An indictment is sufficient if it "(1) states all the elements of the offense charged; (2) informs the defendant of the nature of the charge, enabling the defendant to prepare a defense; and (3) enables the defendant to plead the judgment as a bar to later prosecution for the same offense." United States v. F. J. Vollmer & Co., 1 F.3d 1511, 1518 (7th Cir. 1993), cert. denied, 114 S. Ct. 688 (1994) (citing United States v. James, 923 F.2d 1261, 1265 (7th

Cir. 1991). "Generally, an indictment is sufficient when it sets forth the offense in the words of the statute itself, as long as those words expressly set forth all the elements necessary to constitute the offense intended to be punished." United States v. Hinkle, 637 F.2d 1154, 1157 (7th Cir. 1981); see also United States v. Beard, 713 F. Supp. 285, 289 (S.D. Ind. 1989).

Under this standard, the indictment is insufficient on its face. Each count of the indictment fails to state an essential element of § 1097(a): that the defendant misapplied protected funds "with an intent to injure or defraud the United States." As such, the indictment must be dismissed.

For the reasons stated above, the court GRANTS Mr. Bates' motion to dismiss indictment (filed February 7, 1995 (#19)), and VACATES the status conference scheduled for April 21, 1995.

SO ORDERED.

ENTERED: April 17, 1995

Robert L. Miller, Jr., Judge
United States District Court

cc: R. Hennage; C.R. Oren

11 pp 25
2

ORIGINAL (3)

No. 96-7185

Supreme Court, U.S.
FILED
JAN 16 1997
CLERK

IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1996

GARRIT BATES, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

WALTER DELLINGER
Acting Solicitor General
Department of Justice
Washington, D.C. 20530-0001
(202) 514-2217

4 pp

IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1996

No. 96-7185

GARRIT BATES, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

MEMORANDUM FOR THE UNITED STATES
IN OPPOSITION

Petitioner contends that the court of appeals erred in reversing the order of the district court dismissing the indictment in this case for failing to allege intent to injure or defraud the United States.

1. On September 8, 1994, petitioner was charged in a twelve count indictment returned in the United States District Court for the Northern District of Indiana. The indictment charged that on twelve separate occasions between January 15 and June 15, 1990, petitioner knowingly and willfully misapplied specified amounts of federally guaranteed student loan funds, in violation of 20 U.S.C. 1097(a).[1/] Pet. App. A4.

[1/] At the time of petitioner's charged wrongdoing, 20 U.S.C. 1097(a) declared guilty of a crime "[a]ny person who knowingly and willfully embezzles, misapplies, steals, or obtains by fraud, false statement, or forgery any funds, assets, or property provided or insured under [Title IV of the Higher Education Act of 1965]."

On February 7, 1995, petitioner moved to dismiss the indictment on the ground that a conviction under 20 U.S.C. 1097(a) requires proof of both conversion and the defendant's intent to injure or defraud the United States. On April 7, 1995, the district court granted the motion and dismissed the indictment. The court agreed that Section 1097(a) requires proof of intent to injure or defraud the government. Pet. App. A14-A23.

The court of appeals reversed. Pet. App. A1-A13. It held that intent to injure or defraud the United States is not an element of willful misapplication under Section 1097(a); instead, the government must prove that a defendant misapplied or converted Title IV funds and that he did so knowingly and willfully. Pet. App. A10. The court concluded (Pet. App. A13): "[a]lthough admittedly bareboned, the indictment in this case included all of the requisite elements of willful misapplication under §1097(a), and it certainly alleged sufficient facts to apprise [petitioner] of the charges against him."

2. Petitioner contends (Pet. 4-14) that the government must prove fraudulent intent as an essential element of a Section 1097(a) offense. Whatever the merits of petitioner's contention, it is not presently ripe for review by this Court. The court of appeals' decision places petitioner in precisely the same position he would have occupied if the district court had denied his motion to dismiss. If petitioner is acquitted following a trial on the merits, his contention will be moot. If, on the other hand,

---

petitioner is convicted and his conviction is affirmed on appeal, he will then be able to present his contention to this Court, together with any other claims he may have, in a petition for a writ of certiorari seeking review of a final judgment against him. Accordingly, review by this Court of the court of appeals' decision would be premature at this time.[2/]

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

WALTER DELLINGER
Acting Solicitor General

JANUARY 1997

[2/] Because this case is interlocutory, we are not responding on the merits to the question presented by the petition. We will file a response on the merits if the Court requests.

Supreme Court, U.S.
FILED
APR 11 1997
OFFICE OF THE CLERK

No. 96-7185

In The Supreme Court of the United States

October Term, 1996

Garrit Bates,

Petitioner,

v.

United States of America,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

---

JOINT APPENDIX

C. Richard Oren
(Appointed by this Court)
1104 Main St.
P.O. Box 532
Rochester, IN 46975
(219) 223-9485
Counsel for Petitioner

Walter Dellinger
Acting Solicitor General
Rm 5614, Dept. Of Justice
10 St. & Constitution Ave.
Washington, D.C. 20530
(202) 514-2251
Counsel for Respondent

PETITION FOR CERTIORARI FILED DECEMBER 18, 1996
CERTIORARI GRANTED FEBRUARY 18, 1997

44pp

INDEX

	Page
Chronological List of Relevant Docket Entries	1
Grand Jury Indictment of Garrit Bates Filed September 8, 1994	2
Motion to Dismiss Indictment	13
Judgment Dismissing Indictment	14
Notice of Appeal	15
Memorandum and Order of April 7, 1995 United States District Court, Northern District of Indiana	16
Opinion of the United States Court of Appeals for the Seventh Circuit	25
Judgment of United States Court of Appeals for Seventh Circuit	38
Order of United States Court of Appeals for Seventh Circuit Granting Stay of Mandate	39
Correspondence dated February 28, 1992 from United States Senator Nancy Landon Kassebaum to Mr. James B. Thomas, Jr., Inspector General, United States Dept. of Education	40
Order of the Supreme Court of the United States granting certiorari and leave to proceed in forma pauperis, February 18, 1997	42

CHRONOLOGICAL LIST OF RELEVANT DOCKET ENTRIES

September 8, 1994

The United States files grand jury indictment charging Garrit Bates with twelve (12) counts of Misapplication of Funds in violation of 20 U.S.C. § 1097(a) and 18 U.S.C. § 2.

February 7, 1995

The Defendant, Garrit Bates, files Motion to Dismiss Indictment

April 18, 1995

The United States District Court for Northern District of Indiana, Honorable Robert L. Miller, Judge, enters Judgement granting Defendant's Motion to Dismiss Counts 1 through 12 of the Indictment

May 17, 1995

The United States of America files its Notice of Appeal of Judgement dismissing the indictment against Garrit Bates

September 20, 1996

The United States Court of Appeals enters its Judgement —With Oral Argument, vacating the judgement of the District Court and remanding the cause to the District Court

October 23, 1996

United States Court of Appeals for Seventh Circuit grants the Motion of Garrit Bates to Stay Mandate Pending Petition for Writ of Certiorari to the United States Supreme Court

December 18, 1996

Garrit Bates files his Petition for Writ of Certiorari with the United States Supreme Court

February 18, 1996

The United States Supreme Court enters its Order granting the Petition for Writ of Certiorari and Motion for Leave to Proceed In Forma Pauperis filed by Garrit Bates

UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF INDIANA
SOUTH BEND DIVISION

S Cr. 3:94CR0068RM

UNITED STATES OF AMERICA

v.

GARRIT BATES, a/k/a JERRY BATES

THE GRAND JURY CHARGES:

COUNT 1

At all times material to this indictment:

1. On or about December 17, 1986, James W. and Laurenda Jackson became the owners of the Acme Institute of Technology ("Acme"), a not-for-profit technical school located in South Bend, Indiana. Acme offered associate degree programs in electronics engineering and tool, die and plastics mold design. Acme was licensed by the Indiana Commission on Proprietary Education. The Jacksons appointed JERRY BATES Treasurer of the Board of Trustees of Acme.

2. At the time of the purchase of Acme, James and Laurenda Jackson operated a for-profit firm, Education America, Inc. Education America, Inc. purportedly was a consulting and management firm for vocational/technical schools. BATES was Vice President of Education America, Inc.

3. Students attending Acme were eligible for Guaranteed Student Loans under a program enacted by Congress and administered by the Department of Education. Under this program (found at 20 U.S.C. §§ 1070 *et seq.*) private lenders loaned Acme students money to be used for tuition and other expenses. The Department of Education guaranteed repayment of the loans in the event that the student borrower defaulted. The lending bank submitted the loan proceeds directly to Acme.

4. If a student with a Guaranteed Student Loan withdrew from Acme prior to completion of a term, pursuant to Federal Regulations (34 C.F.R. §§ 682.606 and 668.22), Acme was required to refund a portion of the loan proceeds to the lending institution. The refund amount was considered unearned income. Acme was required to have a fair and equitable refund policy. The amount of the refund was based upon how much of the term had been completed and how much the student had paid the school at the time of withdrawal. Acme's refund policy was incorporated into the Student Enrollment Agreement And Application For Admission signed by each student. The refund policy was also contained in the school catalog. Federal Regulation (34 C.F.R. § 682.607(c)) required that refunds be paid within 30 or 60 days from withdrawal, depending on the date of the loan application. Refunds on Guaranteed Student Loans for unearned tuition were to be paid by Acme directly to the lending institutions. The lending institutions would deduct the refund from the amount owed by the student.

5. On April 30, 1987, Jackson, the President of Acme, signed a Program Participation Agreement with the Department of Education. In that agreement, Jackson agreed to comply with all statutes and regulations governing the Guaranteed Student Loan Program. On January 1, 1990, BATES signed a Program Participation Agreement on behalf of another school operated by Education America, Inc. That school was located in Fort Wayne, Indiana.

6. Beginning in approximately late 1987, Acme began a pattern and practice of not making refunds on Guaranteed Student Loans. The failure of Acme to pay the refunds resulted from decisions made by the Jacksons and BATES.

7. On April 14, 1988, Jackson sent a letter to the Director of Acme which directed him, effective the following month, to "tally the [schools'] receipts for the preceding month and remit a management fee of 10% of [the] total receipts to Education America, Inc." A regular salary for the Jacksons was also to be remitted on a monthly basis. The letter further stated: "If the above creates a cash shortfall in your school, money will be loaned back to you to cover the shortfall." This letter was also sent to the Director of Interstate Technical Institute, located in Ft. Wayne, Indiana, which Jackson purchased on contract in 1986. BATES, as Vice President of Education America had oversight authority at the Interstate Technical Institute.

8. On August 27, 1988, a memorandum from Education America's CEO was sent to the Director of Acme. The memorandum indicated that it was being recommended to Jackson that a full audit be done on Acme due, in part, to unmade refunds. By the end of September 1988, approximately $55,000 was owed on past due guaranteed Student Loan refunds.

9. In late 1988 or early 1989, Education America officials directed Acme to discontinue the use of a special bank account which segregated the unearned income from the general account. This special account was utilized by the former owners of Acme so that funds were always available for timely refunds to the lenders.

10. In January 1989, Acme's Financial Aid Director sent Jackson a letter pointing out the seriousness of the unmade refunds. The letter listed a total refund liability of approximately $68,000.00 owed to various lending institutions.

11. At about this same time, BATES determined on a week-to-week or sometimes day-to-day basis which bills would or would not be paid. BATES had an understanding with the Jacksons that payments to the Jacksons and/or Education America and other bills took priority over payment of refunds. BATES specifically instructed Acme employees not to make student loan refunds.

12. By March 1989, the refund liability had grown to approximately $85,000.00. On March 13, 1989, BATES, as Executive Vice-President of Education America, notified the Financial Aid Director, at her request, that she was released from all responsibility concerning refunds on Guaranteed Student Loans. The letter stated that the refund of any unearned tuition was "solely the responsibility and decision of the corporate office." The Financial Aid Director was told to continue processing new applications and was further advised to continue to prepare refund documents to be approved by the corporation for payment.

13. In May 1989, the National Association of Trade and Technical Schools (NATTS), a national accrediting association, sent its written report following an on-site audit at Acme in April 1989. Accreditation by a national association is required to maintain a technical school's eligibility to participate in the Guaranteed Student Loan program. The report contained a finding that the school had "inadequately demonstrated its ability to make appropriate and timely refunds, [and had also] loaned substantial amounts of money to the chief trustee and a non-related profit making institution." The report also noted evidence of "upstreaming" of management fees to a management company owned by the principle trustee James Jackson.

14. On April 7, 1990, the U.S. Department of Education advised Jackson that effective March 8, 1990, Acme was no longer eligible to participate in the Guaranteed Student Loan Program due to its loss of accreditation.

15. On June 5, 1990, Acme ceased operations and closed its doors.

16. The amount of refunds for unearned income from the Guaranteed Student Loan Program at Acme for the period that BATES was its chief financial officer was approximately $139,649.00, plus interest and special allowances.

17. On or about January 15, 1990, in the Northern District of Indiana,

GARRIT BATES, a/k/a
JERRY BATES,

defendant herein, did knowingly and willfully misapply funds, to-wit: $2,804.23, provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code;

In violation of Title 20, United States Code, Section 1097(a) and Title 18, United States Code, Section 2.

COUNT 2

THE GRAND JURY FURTHER CHARGES:

1. The introductory paragraphs and the allegations in Count 1 of this indictment are herein incorporated by reference.

2. On or about January 16, 1990, in the Northern District of Indiana,

GARRIT BATES, a/k/a
JERRY BATES,

defendant herein, did knowingly and willfully misapply funds, to-wit: $1,566.32, provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code;

In violation of Title 20, United States Code, Section 1097(a) and Title 18, United States Code, Section 2.

COUNT 3

THE GRAND JURY FURTHER CHARGES:

1. The introductory paragraphs and the allegations in Count 1 of this indictment are herein incorporated by reference.

2. On or about January 29, 1990, in the Northern District of Indiana,

GARRIT BATES, a/k/a
JERRY BATES,

defendant herein, did knowingly and willfully misapply funds, to-wit: $714.48, provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code;

In violation of Title 20, United States Code, Section 1097(a) and Title 18, United States Code, Section 2.

COUNT 4

THE GRAND JURY FURTHER CHARGES:

1. The introductory paragraphs and the allegations in Count 1 of this indictment are herein incorporated by reference.

2. On or about April 2, 1990, in the Northern District of Indiana,

GARRIT BATES, a/k/a
JERRY BATES,

defendant herein, did knowingly and willfully misapply funds, to-wit: $903.73, provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code;

In violation of Title 20, United States Code, Section 1097(a) and Title 18, United States Code, Section 2.

COUNT 5

THE GRAND JURY FURTHER CHARGES:

1. The introductory paragraphs and the allegations in Count 1 of this indictment are herein incorporated by reference.

2. On or about April 27, 1990, in the Northern District of Indiana,

GARRIT BATES, a/k/a
JERRY BATES,

defendant herein, did knowingly and willfully misapply funds, to-wit: $1,940.00, provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code;

In violation of Title 20, United States Code, Section 1097(a) and Title 18, United States Code, Section 2.

COUNT 6

THE GRAND JURY FURTHER CHARGES:

1. The introductory paragraphs and the allegations in Count 1 of this indictment are herein incorporated by reference.

2. On or about April 27, 1990, in the Northern District of Indiana,

GARRIT BATES, a/k/a
JERRY BATES,

defendant herein, did knowingly and willfully misappy funds, to-wit: $2,156.14, provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code;

In violation of Title 20, United States Code, Section 1097(a) and Title 18, United States Code, Section 2.

COUNT 7

THE GRAND JURY FURTHER CHARGES:

1. The introductory paragraphs and the allegations in Count 1 of this indictment are herein incorporated by reference.

2. On or about May 7, 1990, in the Northern District of Indiana,

GARRIT BATES, a/k/a
JERRY BATES,

defendant herein, did knowingly and willfully misapply funds, to-wit: $1,660.80, provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code;

In violation of Title 20, United States Code, Section 1097(a) and Title 18, United States Code, Section 2.

COUNT 8

THE GRAND JURY FURTHER CHARGES:

1. The introductory paragraphs and the allegations in Count 1 of this indictment are herein incorporated by reference.

2. On or about May 11, 1990, in the Northern District of Indiana,

GARRIT BATES, a/k/a
JERRY BATES,

defendant herein, did knowingly and willfully misapply funds, to-wit: $675.13, provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code;

In violation of Title 20, United States Code, Section 1097(a) and Title 18, United States Code, Section 2.

COUNT 9

THE GRAND JURY FURTHER CHARGES:

1. The introductory paragraphs and the allegations in Count 1 of this indictment are herein incorporated by reference.

2. On or about May 18, 1990, in the Northern District of Indiana,

GARRIT BATES, a/k/a
JERRY BATES,

defendant herein, did knowingly and willfully misapply funds, to-wit: $1,940.00, provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code;

In violation of Title 20, United States Code, Section 1097(a) and Title 18, United States Code, Section 2.

COUNT 10

THE GRAND JURY FURTHER CHARGES:

1. The introductory paragraphs and the allegations in Count 1 of this indictment are herein incorporated by reference.

2. On or about June 9, 1990, in the Northern District of Indiana,

GARRIT BATES, a/k/a
JERRY BATES,

defendant herein, did knowingly and willfully misapply funds, to-wit: $1,486.47, provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code;

In violation of Title 20, United States Code, Section 1097(a) and Title 18, United States Code, Section 2.

COUNT 11

THE GRAND JURY FURTHER CHARGES:

1. The introductory paragraphs and the allegations in Count 1 of this indictment are herein incorporated by reference.

2. On or about June 12, 1990, in the Northern District of Indiana,

GARRIT BATES, a/k/a
JERRY BATES,

defendant herein, did knowingly and willfully misapply funds, to-wit: $779.69, provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code;

In violation of Title 20, United States Code, Section 1097(a) and Title 18, United States Code, Section 2.

COUNT 12

THE GRAND JURY FURTHER CHARGES:

1. The introductory paragraphs and the allegations in Count 1 of this indictment are herein incorporated by reference.

2. On or about June 15, 1990, in the Northern District of Indiana,

GARRIT BATES, a/k/a
JERRY BATES,

defendant herein, did knowingly and willfully misapply funds, to-wit: $474.28, provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code;

In violation of Title 20, United States Code, Section 1097(a) and Title 18, United States Code, Section 2.

A TRUE BILL

/s/ Karen Burns
Foreperson

JON E. DEGUILIO
United States Attorney

By: /s/ Ruth M. Hennage
RUTH M. HENNAGE
Assistant United States Attorney

UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF INDIANA
SOUTH BEND DIVISION

(Caption Omitted)

MOTION TO DISMISS

The defendant, Garrit Bates, through undersigned counsel, pursuant to rule of Criminal Procedure 12(b)(2), moves the court for an order dismissing the indictment filed herein on September 8th, 1994, on the ground that the indictment fails to set forth essential facts which constitute a criminal offense under 20 U.S.C. 1097(a).

Respectfully Submitted,

/s/ C. Richard Oren
C. RICHARD OREN #15074-25
Attorney for Defendant
1104 Main Street
Rochester, IN 46975
Telephone: (219) 223-9485
Attorney for Defendant

(Certificate of Service Omitted)

UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF INDIANA

(Caption Omitted)

JUDGMENT

This action came before the court, United States District Judge Robert L. Miller, Jr. presiding. The decision having been duly rendered, it is ordered and adjudged.

That defendant's motion to dismiss counts 1 through 12 of the indictment is GRANTED.

This document entered pursuant to Rules 79(A) and 58 of the Federal Rules of Civil Procedure on: April 18, 1995

By: /s/ Geraldine J. Crockett
GERALDINE J. CROCKETT
Deputy Clerk of the Court

UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF INDIANA
SOUTH BEND DIVISION

(Caption Omitted)

NOTICE OF APPEAL

Notice is hereby given that the United States of America, plaintiff above named, hereby appeals to the United States Court of Appeals for the Seventh Circuit from the Judgment on Decision by the Court dismissing the indictment against Garrit Bates, entered in this action on the 18th day of April, 1995.

JON E. DEGUILIO
United States Attorney

By: /s/ Ruth M. Hennage
RUTH M. HENNAGE
Assistant United States Attorney
M01 Federal Building
204 S. Main Street
South Bend, IN 46601-2191
219/236-8287

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF INDIANA
SOUTH BEND DIVISION

(Caption Omitted)

MEMORANDUM AND ORDER

Defendant Garrit Bates' moves to dismiss the indictment against him and for oral argument. Because the parties have adequately briefed the motion to dismiss, the court denies the motion for oral argument. For the following reasons, the court grants the motion to dismiss.

Mr. Bates was indicted on September 8, 1994 on twelve counts of aiding and abetting the knowing and willful misapplication of federally insured funds pursuant to 20 U.S.C. § 1097(a), 18 U.S.C. § 2. Mr. Bates contends that the facts alleged in the indictment could not support a finding that the essential elements of § 1097(a) have been met. The government disagrees both with Mr. Bates's version of the essential elements and with his conclusion that the indictment fails to allege facts that could satisfy those essential elements.

The indictment charges that Mr. Bates was the Treasurer of the Board of Trustees of the Acme Institute of Technology, a not-for-profit technical school owned by James and Laurenda Jackson. Mr. Bates also was Vice-President of Education America, Inc., which the Jacksons also owned.

Acme students were eligible for guaranteed student loans ("GSLs") under a program enacted by Congress and administered by the Department of Education. If a student withdrew from Acme before a term's completion, federal regulations required Acme to refund a portion of

loan proceeds to the lending institution. Federal regulations required that the refunds be paid within 30 or 60 days of the student's withdrawal.

The indictment charges that beginning in 1987, decisions made by the Jacksons and Mr. Bates resulted in Acme beginning a practice of not making refunds on GSLs. In late 1988 or 1989, Education America officials directed Acme to discontinue the use of a special bank account that segregated the refunds from the general account. Around January 1989, according to the indictment, Mr. Bates determined on a week-to-week, or sometimes day-to-day, basis which bills would or would not be paid with the understanding that payments to the Jacksons took precedence over payment of refunds. The indictment alleges that Mr. Bates specifically instructed Acme employees not to make student loan refunds.

On March 13, 1989, Mr. Bates, as Executive Vice-President of Education America, allegedly notified the Financial Aid Director that, pursuant to her request, she was released from all responsibility concerning refunds on GSLs. The letter stated that the refund of any unearned tuition was "solely the responsibility and decision of the corporate office." The Financial Aid Director allegedly was directed, however, to continue to prepare refund documents to be approved by the corporation for payment.

Effective March 8, 1990, Acme no longer was eligible to participate in the GSL program because Acme had lost its accreditation from the National Association of Trade and Technical Schools. On June 5, 1990, Acme ceased operation and closed its doors; at that time, the amount of unrefunded GSL funds allegedly had accrued to a total of $139,649.00 while Mr. Bates was chief financial officer at Acme.

The indictment then charges, in twelve different counts, that on January 15, January 16, January 29, April 2,

twice on April 27, May 7, May 11, May 18, June 9, June 12 and June 15 of 1990, Mr. Bates knowingly and willfully misapplied funds provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code in violation of 20 U.S.C. § 1097(a) and 18 U.S.C. § 2.

The indictment charges Mr. Bates with crimes occurring in 1990. At that time, 20 U.S.C. § 1097(a) defined criminal conduct as follows: "Any person who knowingly and willfully embezzles, misapplies, steals, obtains by fraud, false statement or forgery any funds . . . provided or insured under this subchapter . . . ."

Mr. Bates relies upon *United States v. Kammer*, 1 F.3d 1161, 1165 (11th Cir. 1993), to argue that, with respect to a charge under § 1097(a), "[t]o establish a criminal misapplication, the government must prove (1) a conversion of the property to the use of the defendant or a third party, and (2) fraudulent intent." *United States v. Kammer*, 1 F.3d at 1165. Mr. Bates contends that the indictment does not allege facts supporting these essential elements.

The government responds that the *Kammer* court's interpretation of the essential elements of § 1097(a) is erroneous. The government contends that the elements necessary to prove the charge of misapplication of funds under § 1097(a) are: (1) that the funds described in the indictment were provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code at the time alleged; (2) that the defendant misapplied such funds; and (3) that he did so knowingly and willfully. The government defines "misapplication" to mean a conversion of funds to the defendant's own use or the use of another.

The government's version of the essential elements restates the elements as they are stated in § 1097(a), but the controversy between Mr. Bates and the government lies in the definition of misapplication of funds. Both parties argue, and the court agrees, that a misapplication

requires a conversion, but the parties dispute whether a misapplication under § 1097(a) also requires fraudulent intent.

The government contends that the Seventh Circuit does not always require an intent to defraud with respect to statutes that forbid "misapplication of funds," citing *United States v. Brown*, 742 F.2d 363 (7th Cir. 1984). Applying 18 U.S.C. § 665 of the Comprehensive Employment and Training Act ("CETA"), the *Brown* court stated that:

> In *United States v. Tamargo*, 637 F.2d 346[, 350] (5th Cir.), *cert. denied*, 454 U.S. 824 (1981), the court approved the trial court's use of a jury instruction that stated that "misapplication of funds" for purposes of § 665 meant the conversion of funds to the defendant's own use or the use of another.

742 F.2d at 366. The *Brown* court said no more regarding the term's definition. The *Brown* court, however, omitted a critical clause from *Tamargo*'s definition of misapplication of funds, for *Tamargo* actually states that, "The trial court here properly charged the jury to "misapply money or property means a willful conversion or taking of such money or property to one's own use and benefit or the use and benefit for another, *with intent to defraud*." *United States v. Tamargo*, 637 F.2d at 350 (emphasis added). Accordingly, the quoted language from the *Brown* case has little influence.

Nevertheless, the court is hesitant to follow the *Kammer* case. The essential elements stated in the *Kammer* case were derived from *United States v. Jakeway*, 783 F. Supp. 590, 597 (M.D. Fla. 1992), in which the court explained that although the Eleventh Circuit had not defined "misapplication" in the context of § 1097(a), the term had been defined in the context of 18 U.S.C. § 656, which deals with misapplication of funds by a bank officer or employee. *United States v. Jakeway*, 783 F. Supp. at 597, n. 6. Thus, the *Jakeway* court extrapolated the ele-

ments of criminal misapplication from *United States v. Acosta*, 748 F.2d 577, 580 (11th Cir. 1984), which held that misapplication under 18 U.S.C. § 656 is the "willful taking of an insured bank's money by its employee with intent to defraud the bank." *United States v. Acosta*, 748 F.2d at 580. Therefore, the *Kammer* holding is founded upon an earlier holding that, under a different statute, misapplication required fraudulent intent.

The Seventh Circuit has not defined "misapplication" with respect to § 1097(a), but, like the Eleventh Circuit, requires a finding of intent to defraud or injure with respect to misapplication of bank funds under 18 U.S.C. § 656. *United States v. Crabtree*, 979 F.2d 1261, 1266 (7th Cir. 1992), *cert. denied*, 114 S. Ct. 217 (1993) (to prove a violation of 18 U.S.C. § 656, the government must prove, among other things, that the defendant willfully misapplied funds of the bank with the intent to injure or defraud the bank).

This does not necessarily compel a conclusion that § 1097(a) also requires fraudulent intent. The fraudulent intent element required under 18 U.S.C. § 656 has a historical basis in the statute itself:

> The current statutory language does not expressly require any proof of intent. Originally the statute did require proof of intent to "injure or defraud" the bank or "deceive" a bank officer but these words were inadvertently dropped in the course of a technical revision of the criminal code. To avoid making every unauthorized loan by a bank officer a willful misapplication of bank funds, courts, including our own, read the missing words back into the statute.

United States v. Bates, 852 F.2d 212, 215 (7th Cir. 1988); *see also United States v. Angelos*, 763 F.2d 859, 861 (7th Cir. 1985); *United States v. Shively*, 715 F.2d 260, 266 (7th Cir. 1983), *cert. denied*, 465 U.S. 1007 (1984) ("these words were dropped by a reviser without intent to alter the meaning of the law").

In *United States v. Garcia*, 751 F.2d 1033 (9th Cir. 1985), however, the Ninth Circuit affirmed the dismissal of an indictment for "wilfully misappl[ying]" CETA funds in violation of 18 U.S.C. § 665 because the government conceded it could not prove intent to injure or defraud. *United States v. Garcia*, 751 F.2d at 1034. In concluding that § 665 requires a specific intent to injure or defraud, the district court had relied on the Ninth Circuit's interpretation of the bank fraud statute, 18 U.S.C. § 656. *Id.* at 1036. On appeal, the government contended that the analogy between § 656 and § 665 was not compelling because, as discussed above, the original version of § 656 expressly required an intent to injure and defraud the bank, and Congress had expressly disclaimed any intention of changing the law. *Id.* The Ninth Circuit rejected this contention, stating:

> But this circumstance cuts against the government's reading of the statute. The only reason Congress could have considered the explicit requirement of a purpose to injure or defraud redundant was that Congress understood the term "willful misapplication" to include such an intent by implication.

Id.

Thus, the Ninth Circuit held that a "willful misapplication" for the purposes of § 665 necessarily includes an intent to defraud or injure. In doing so, the court reasoned that:

> In a criminal statute, "willfully" generally means a voluntary, intentional violation of a known legal duty in bad faith or with evil purpose. *See United States v. Pomponio*, 429 U.S. 10, 11-12 (1976) (per curiam); *United States v. Bishop*, 412 U.S. 346, 260 (1973). A general intent to commit the proscribed act is not enough; a specific intent to do something the law forbids is required. *See United States v. Wilson*, 631 F.2d 118, 119 (9th Cir. 1980). The definition of "misapplication" suggests

> a similar element: "[i]mproper, illegal, wrongful, or corrupt use [or] application of funds, property, etc." Black's Law Dictionary 901 (5th Ed. 1979).

Id. at 1035; *see also Morissette v. United States*, 342 U.S. 246, 276 (1952) (holding that "knowingly converts" under 18 U.S.C. § 641 required an intention "wrongfully to deprive another of possession of property.").

The Ninth Circuit gave much importance to the fact that the term "willfully misapply" in 18 U.S.C. § 665(a) "is embedded in a series of words referring to harmful or wrongful acts clearly causing financial injury to the United States or impeding the achievement of CETA's goals. All the acts prohibited by the statute are more serious in character than simple violations of procedural requirements." *United States v. Garcia*, 751 F.2d at 1035-36; *see also United States v. Hammen*, 977 F.2d 379, 384 (7th Cir. 1992) (in a 18 U.S.C. § 656 case, "[t]he intent to defraud or injure the bank is what separates criminal misapplication from mere maladministration."); *United States v. Bates*, 852 F.2d at 215 (stating that courts read the intent to defraud or injure back into 18 U.S.C. § 656 "[t]o avoid making every unauthorized loan by a bank officer a willful misapplication of bank funds.").

Similarly, the term "misapply" in § 1097(a) "is embedded in a series of words referring to harmful or wrongful acts clearly causing financial injury to the United States . . ." *United States v. Garcia*, 751 F.2d at 1035. Further, as was the case in *Garcia* under 18 U.S.C. § 665, "[a]ll the acts prohibited by [§ 1097(a)] are more serious in character than simple violations of procedural requirements." *United States v. Garcia*, 751 F.2d at 1036.

The court finds the reasoning of *Garcia* persuasive, and thus elects to follow the course of *United States v. Kammer*, 1 F.3d 1161 in holding that, with respect to

a charge under § 1097(a), "[t]o establish a criminal misapplication, the government must prove (1) a conversion of the property to the use of the defendant or a third party, and (2) fraudulent intent." *United States v. Kammer*, 1 F.3d at 1165. Thus, the essential elements of a willful and knowing misapplication under § 1097(a) include: (1) that the funds described in the indictment were provided and insured under subchapter IV of Chapter 28 of Title 20 of the United States Code at the time alleged; (2) that the defendant willfully and knowingly misapplied such funds; and (3) that he did so with an intent to injure or defraud the United States. A defendant misapplies funds by converting them to the defendant's own use or the use of another.

Mr. Bates contends that the indictment is defective because it does not allege facts supporting a finding that the defendant's actions constitute violations of § 1097(a). He contends that the indictment fails to recite all of the essential elements of a willful and knowing misapplication under § 1097(a). An indictment is sufficient if it "(1) states all the elements of the offense charged; (2) informs the defendant of the nature of the charge, enabling the defendant to prepare a defense; and (3) enables the defendant to plead the judgment as a bar to later prosecution for the same offense." *United States v. F. J. Vollmer & Co.*, 1 F.3d 1511, 1518 (7th Cir. 1993), *cert. denied*, 114 S. Ct. 688 (1994) (citing *United States v. James*, 923 F.2d 1261, 1265 (7th Cir. 1991). "Generally, an indictment is sufficient when it sets forth the offense in the words of the statute itself, as long as those words expressly set forth all the elements necessary to constitute the offense intended to be punished." *United States v. Hinkle*, 637 F.2d 1154, 1157 (7th Cir. 1981); *see also United States v. Beard*, 713 F. Supp. 285, 289 (S.D. Ind. 1989).

Under this standard, the indictment is insufficient on its face. Each count of the indictment fails to state an

essential element of § 1097(a): that the defendant misapplied protected funds "with an intent to injure or defraud the United States." As such, the indictment must be dismissed.

For the reasons stated above, the court GRANTS Mr. Bates' motion to dismiss indictment (filed February 7, 1995 (#19)), and VACATES the status conference scheduled for April 21, 1995.

SO ORDERED.

ENTERED: April 17, 1995

/s/ Robert L. Miller, Jr.
ROBERT L. MILLER, JR.
Judge
United States District Court

cc: R. Hennage; C.R. Oren

IN THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

No. 95-2203

UNITED STATES OF AMERICA,
Plaintiff-Appellant,
v.
GARRIT BATES,
Defendant-Appellee.

Argued February 12, 1996—Decided September 20, 1996

Before CUDAHY, FLAUM, and KANNE, *Circuit Judges.*

KANNE, *Circuit Judge.* After Garrit Bates was charged with twelve counts of willfully misapplying federally guaranteed Title IV student aid funds, he filed a pretrial motion to dismiss the indictment as insufficient. Specifically, he argued that both conversion and intent to injure or defraud the federal government are elements of the offense of willfully misapplying financial aid monies and that the indictment had failed to adequately allege either one. The district court granted his motion to dismiss after determining that the indictment failed to allege intent to injure or defraud the United States, and the government appeals to this court. Because we find that a conviction for willful misapplication of Title IV funds does not require proof of the defendant's intent to injure or defraud the United States, and that the indictment is otherwise sufficient, we vacate the judgment of the district court and reinstate the prosecution.

I. History

Given that the district court determined that the indictment was insufficient on its face, for this appeal we take the facts as they are alleged in the indictment, which are set out below. James and Laurenda Jackson are the owners and operators of Education America, Inc., a for-profit consulting and management firm for various technical and vocational schools. In December 1986, the Jacksons acquired ownership of the Acme Institute of Technology, a not-for-profit technical school located in South Bend, Indiana. After the acquisition, the Jacksons appointed Bates, who was vice president of Education America at the time, to act as Acme's chief financial officer and treasurer of the Acme board of trustees.

On April 30, 1987, Mr. Jackson, acting as president of Acme, signed a program participation agreement with the Department of Education. Under the agreement, Acme became authorized to receive student loan checks through the Title IV federal Guaranteed Student Loan ("GSL") program, but participation in the program was contingent upon (1) Acme's continued accreditation by an approved accrediting association, and (2) Jackson's promise to comply with all statutes and regulations governing the GSL program. Around the same time, Bates signed a similar participation agreement for a different school owned by Education America, and he therefore presumably understood the responsibilities imposed by the Acme participation agreement.

Through the GSL program, banks and other private financial institutions would lend money to Acme students for tuition and other educational expenses. The federal government's role was to administer the loan program and guarantee payment of the loans in the event any of the student borrowers defaulted. Loan checks were mailed directly to Acme and, once endorsed, were credited against the student's tuition debt. However, if a student with a GSL withdrew from Acme prior to completion of a term,

federal regulations required Acme to refund a portion of the loan proceeds to the lender within 30 or 60 days from withdrawal (depending on the date of the loan application), which was then to be deducted from the amount owed. Of course, if loan refunds were not made, the student—and, in the event of default, the government—would nonetheless remain liable to the lender for the full amount of the loan.

On April 14, 1988, Mr. Jackson sent a letter to the director of Acme instructing him (1) to remit 10 percent of Acme's gross receipts from the previous month to Education America as a management fee, and (2) to arrange for a specified monthly salary to be paid by Acme to the Jacksons. The letter explained that if these required payments caused Acme to experience a cash shortfall, Education America would loan money back to Acme in order to cover the discrepancy. As chief financial officer of Acme, Bates had the authority to determine which of Acme's bills would be paid as they came due, and he repeatedly gave these fee and salary payments to Education America and the Jacksons priority over refunds to lenders of student loan monies for withdrawn students. In doing this, Bates would specifically direct Acme employees not to make required student loan refunds. By the end of September 1988, Acme had amassed a GSL refund debt of approximately $55,000.

In late 1988 or very early 1989, Education America officials directed Acme to discontinue using a special bank account that was designed to segregate unearned student loan monies (those that should have been earmarked for refunds) from the school's general funds account. When Acme's refund arrearage had grown to around $68,000 by January 1989, Acme's financial aid director sent a letter to Mr. Jackson frustratedly pointing out the seriousness of failing to pay refunds of Title IV monies. In March 1989, Acme's unpaid student loan refunds totaled $85,000. That month, Bates notified Acme's financial aid director,

at her request, that she was absolved of all legal responsibility concerning refunds on GSLs and that such funds would be "solely the responsibility and decision of the corporate office."

In April 1989, the National Association of Trade and Technical Schools ("NATTS"), a national accrediting association, performed an on-site audit of Acme for the purpose of determining whether it should continue to accredit the school. In its May 1990 report to the Department of Education, NATTS found that Acme had "inadequately demonstrated its ability to make appropriate and timely refunds," and that it had "loaned substantial amounts of money" and engaged in the "upstreaming" of management fees to Education America and its owner, Mr. Jackson, who also happened to be Acme's president and chairman of the board of trustees.

After losing its accreditation, Acme received notice from the Department of Education that effective March 8, 1990, Acme was no longer eligible to participate in the GSL program. On June 5, 1990, Acme closed its doors, having accrued a total student loan refund debt of $139,649, not including interest and certain special allowances.

On September 8, 1994, a federal grand jury handed down a twelve-count indictment against Bates. Following a recitation of the facts set out above, the indictment charges that on twelve separate occasions between January 15 and June 15, 1990, Bates knowingly and willfully misapplied specified amounts of federally guaranteed student loan funds, in violation of 20 U.S.C. § 1097 and 18 U.S.C. § 2. At the time of Bates's alleged wrongdoing in 1990, § 1097(a) declared guilty of a crime "[a]ny person who knowingly and willfully embezzles, misapplies, steals, or obtains by fraud, false statement, or forgery any funds, assets, or property provided or insured under [Title IV of the Higher Education Act of 1965] . . . ." 20 U.S.C. § 1097(a).

On February 7, 1995, Bates filed a motion to dismiss the indictment. The memorandum in support of his motion argued first that conviction under § 1097(a) for willful misapplication of student aid funds requires proof of both conversion and the defendant's intent to injure or defraud the United States, and second, that the indictment failed to allege sufficient facts to constitute conversion and neglected to allege intent to injure or defraud the United States at all. The district court agreed that § 1097(a) requires proof of the intent to injure or defraud the government and that the indictment had failed to allege such intent, and it therefore granted the motion and dismissed the indictment.

II. Analysis

The government appeals from the judgment of dismissal, arguing (1) that a conviction for willful misapplication of Title IV funds does not require that the government demonstrate the defendant's intent to injure or defraud the United States, and (2) that regardless of whether § 1097(a) requires a showing of such intent, the indictment was facially sufficient. We address these separate arguments in turn. Our review of a district court's determination concerning the facial sufficiency of an indictment is *de novo*. *Frank v. United States*, 914 F.2d 828, 830 (7th Cir. 1990) (citing *United States v. Bucey*, 876 F.2d 1297, 1301-02 (7th Cir.), *cert. denied*, 493 U.S. 1004 (1989)). We likewise engage in plenary review of a district court's statutory interpretation. *United States v. Shriver*, 980 F.2d 456, 459 (7th Cir. 1992).

A. Intent to Injure or Defraud the United States

A basic tenet of criminal law provides that *actus non facit reum nisi mens sit rea*, meaning an act does not make one guilty unless his mind is guilty. Thus, at common law, nearly all crimes required proof that the defendant not only committed a wrongful act, but that he did

so with the requisite *mens rea*, or culpable mental state. As history has witnessed the statutory codification of criminal offenses, enacting legislatures have employed such words as "intentionally," "willfully," or "purposefully" to signifiy the common law requirement of mental culpability. *See Morissette v. United States*, 342 U.S. 246, 251-52, 72 S. Ct. 240, 244 (1952).

But criminal intent (even when differentiated from such other, lesser mental states as objective knowledge, recklessness, or negligence) is an elusive concept—some crimes may demand proof of only the defendant's *general* intent to engage consciously and voluntarily in the proscribed conduct, while other crimes may additionally require proof of the defendant's *specific* intent to effectuate a particular result. 1 WAYNE R. LAFAVE & AUSTIN W. SCOTT, JR., SUBSTANTIVE CRIMINAL LAW § 3.5, at 302-18 (1986 & Supp. 1996). On this appeal, we must reach the question we declined to answer in *United States v. Ross*, 77 F.3d 1525, 1546 (7th Cir. 1996): whether conviction under 20 U.S.C. § 1097(a) for willfully misapplying federally insured student aid funds requires the government to allege and prove the defendant's specific intent to injure or defraud the United States.

In *Morissette*, the Supreme Court instructed:

> [W]here Congress borrows terms of art in which are accumulated the legal tradition and meaning of centuries of practice, it presumably knows and adopts the cluster of ideas that were attached to each borrowed word in the body of learning from which it was taken and the meaning its use will convey to the judicial mind unless otherwise instructed.

342 U.S. at 263, 72 S. Ct. at 250. Congress has utilized the expression "willful misapplication" in a host of criminal statutory provisions. And thus, although few of these crimes are (as in *Morissette*) centuries old, we have much

to which we may turn by way of analogy in discerning the elements of willful misapplication, as the term is used in § 1097(a).

Bates contends, citing *United States v. Kammer*, 1 F.3d 1161, 1165 (11th Cir. 1993),* and *United States v. Jakeway*, 783 F. Supp. 590, 597 (M.D. Fla. 1992), that we should look for guidance to our interpretation of 18 U.S.C. § 656, which prohibits bank insiders from, among other things, willfully misapplying the bank's funds. This court, like the Eleventh and most of our other sister circuits, has defined the crime of willfully misapplying bank funds to require proof (1) that the defendant intentionally converted bank funds to his own use or the use of another, and (2) that the defendant did so with the specific intent to injure or defraud the bank. *United States v. Crabtree*, 979 F.2d 1261, 1266-67 (7th Cir. 1992), *cert. denied*, 510 U.S. 878 (1993); *United States v. Bruun*, 809 F.2d 397, 408 (7th Cir. 1987). Either the intent to injure *or* the intent to defraud will suffice, and they are not the same. *United States v. Bates*, 852 F.2d 212, 215 (7th Cir. 1988); *United States v. Angelos*, 763 F.2d 859, 861 (7th Cir. 1985). For the defendant to have acted with the intent to injure the bank, "it is sufficient that the loan officer engaged in acts, the natural tendency of which would be to injure the bank." *Crabtree*, 979 F.2d at 1268 (quoting *Bruun*, 809 F.2d at 408). Intent to defraud the bank, on the other hand, "means to take financial advantage of a confidential relationship and does not require any intent to injure the bank." *Bates*, 852 F.2d at 215-16 (citing *Angelos*, 763 F.2d at 861-62).

The government concedes that willful misapplication of federally guaranteed student aid funds requires the defend-

---

* Because this opinion conflicts with the Eleventh Circuit's holding in *Kammer*, it was circulated before release to all judges in active service pursuant to 7th Cir. R. 40(e). No judge requested a rehearing en banc.

ant to have intentionally converted such funds to his own use or the use of a third party, but it argues that the defendant's specific intent to injure or defraud the United States is not an element of the offense. We agree.

The mere fact that we have interpreted willful misapplication of bank funds to require both intentional conversion *and* the intent to injure or defraud the bank does not necessitate the conclusion that specific fraudulent or injurious intent is part and parcel of "willful misapplication." In fact, quite the opposite is true. Intent to injure or defraud the bank is not subsumed within the phrase "willful misapplication," but rather is a separate and distinct component of § 656. *See Crabtree*, 979 F.2d at 1266 (noting that § 656 requires both "that the defendant willfully misapplied funds of the bank" and that he did so "with the intent to injure or defraud the bank"). The point is further illustrated by the Fifth Circuit's recent approval of the following instructions in a bank fund misapplication case:

> To willfully misapply a bank's money or property means an intentional conversion of such money or property to one's own use and benefit, or for the use and benefit of another, knowing that one had no right to do so.
>
> To act with the intent to defraud means to act with an intent to deceive or cheat someone, ordinarily for the purpose of causing some financ[ial] loss to another or bringing about some financial gain to oneself.

United States v. Giraldi, No. 94-60602, 1996 WL 339177, at *8 (5th Cir. June 19, 1996). Thus, intent to injure or defraud is an offense element that must be proved *in addition to* willful misapplication in a § 656 prosecution.

It is true that the language of § 656, like that of § 1097(a), does not explicitly require the defendant to have acted with specific fraudulent or injurious intent.

However, there is a historical rationale for reading into § 656 the requirement of the defendant's intent to injure or defraud the bank. In *Bates*, we explained:

> The current statutory language does not expressly require any proof of [fraudulent or injurious] intent. Originally the statute did require proof of intent to "injure or defraud" the bank or "deceive" a bank officer but these words were inadvertently dropped in the course of a technical revision of the criminal code. To avoid making every unauthorized loan by a bank officer a willful misapplication of bank funds, courts, including our own, read the missing words back into the section.

852 F.2d at 215 (citing *Angelos*, 763 F.2d at 861; *United States v. Shively*, 715 F.2d 260, 266 (7th Cir. 1983), *cert. denied*, 465 U.S. 1007 (1984)). Section 1097(a) has never included a requirement that the defendant have acted with an intent to injure or defraud the government, and with no textual or historical basis for doing so, we are reluctant to read such a requirement into the statute.

Our reluctance is bolstered by this circuit's prior analysis of 18 U.S.C. § 665, another statute prohibiting the willful misapplication of federal funds—specifically, Comprehensive Employment and Training Act ("CETA") funds. In *United States v. Hamilton*, a defendant charged under § 665 with willful misapplication of CETA funds argued that he could not be convicted because he did not know the monies he misapplied were federal funds. 726 F.2d 317, 320 (7th Cir. 1984). Under § 656, a defendant cannot be convicted if he did not know the funds were the bank's because he must have acted with intent to injure or defraud the bank, and thus Hamilton urged this court to pattern our interpretation of § 665's requirements after those of § 656. *Id.* We refused to employ such an analogy, explaining that "we need not wander that far

afield, since a closer analogy is found in the general selection concerning embezzlement of public money, 18 U.S.C. § 641." *Id.* (citing *United States v. Coleman*, 590 F.2d 228 (7th Cir. 1978), *cert. denied*, 440 U.S. 980 (1979)).

Section 641, as construed in *Morissette*, requires only that the defendant intentionally converted public funds to his own use and benefit or to that of a third person. 342 U.S. at 263, 270-72, 72 S. Ct. at 250, 254. Thus, in *United States v. Brown*, we held that " 'misapplication of funds' for purposes of § 665 mean[s] the conversion of funds to the defendant's own use or the use of another," and that "the conversion of CETA funds for the use of uncertified workers when the defendant knows of their uncertified status is a willful misapplication of funds for purposes of § 665." 742 F.2d 363, 366-67 (7th Cir. 1984). *But see United States v. Garcia*, 751 F.2d 1033, 1037 (9th Cir. 1985) (holding that intent to injure or defraud the United States is an essential element of willful misapplication under § 656-esque requirement that the defendant have acted with intent to injure or defraud the United States, holding:

> We believe that Congress, through § 665, desired to afford federal protection to the large sums of federal money entrusted to nonfederal agencies to accomplish the purposes of CETA, and did not intend to limit this protection to situations where the defendant was aware of a federal interest in the funds.

726 F.2d at 320. This reasoning applies equally here, where Congress has sought through § 1097(a) to provide broad protection for Title IV student financial aid funds entrusted to private educational institutions.

We conclude, therefore, that intent to injure or defraud the United States is not an element of willful misapplication under § 1097(a). Rather, the government must prove that the defendant misapplied—i.e., converted—Title IV

funds and that he did so knowingly and willfully. The Supreme Court has defined willfulness as the "voluntary, intentional violation of a known legal duty." *United States v. Pomponio*, 429 U.S. 10, 12-13, 97 S. Ct. 22, 24 (1976). Conversion is an "unprivileged interference with the owner's possession and enjoyment of a chattel." *Kerrigan v. American Orthodontics Corp.*, 960 F.2d 43, 45 (7th Cir. 1992); *see also Ross*, 77 F.3d at 1546 (quoting *Kammer*'s definition of conversion as "an act of dominion or control over the property that seriously interferes with the owner's rights," 1 F.3d at 1165). *Morissette* explained:

> Conversion . . . may be consummated without any intent to keep and without any wrongful taking, where the initial possession by the converter was entirely lawful. Conversion may include misuse or abuse of property. It may reach use in an unauthorized manner or to an unauthorized extent of property placed in one's custody for limited use. Money rightfully taken into one's custody may be converted without any intent to keep or embezzle it merely by commingling it with the custodian's own, if he was under a duty to keep it separate and intact.

342 U.S. at 271-72, 72 S. Ct. at 254. Thus, as a working definition, willful misapplication under § 1097(a) requires the government to allege and prove that the defendant consciously, voluntarily, and intentionally exercised unauthorized control or dominion over federally provided or guaranteed Title IV funds that interfered with the rights of the funds' true owner(s), for the use and benefit of the defendant or a third person, while knowing that such an exercise of control or dominion over the funds was a violation of the law.

B. Sufficiency of the Indictment's Allegation of Conversion

In his motion to dismiss, reiterated on appeal, Bates argued that the indictment was insufficient first because it did not allege intent to injure or defraud the government, and second because it failed to allege sufficient facts to constitute conversion. Having decided that intent to injure or defraud is not an element of § 1097(a), this leaves only Bates's argument that the indictment failed to adequately charge conversion.

Facial sufficiency is not a high hurdle. Indictments need not exhaustively describe the facts surrounding a crime's commission nor provide lengthy explanations of the elements of the offense. FED. R. CRIM. P. 7(c)(1) instructs that "[t]he indictment or the information shall be a plain, concise and definite written statement of the essential facts constituting the offense charged." We have held that "[a]n indictment is sufficient if it: (1) states all the elements of the offense charged; (2) informs the defendant of the nature of the charge, enabling the defendant to prepare a defense; and (3) enables the defendant to plead the judgment as a bar to later prosecution for the same offense." *U.S. v. F.J. Vollmer & Co., Inc.*, 1 F.3d 1511, 1518 (7th Cir. 1993) (citing *United States v. James*, 923 F.2d 1261, 1265 (7th Cir. 1991)), *cert. denied*, 114 S. Ct. 688 (1994). "Generally, an indictment is sufficient when it sets forth the offense in the words of the statute itself, as long as those words expressly set forth all the elements necessary to constitute the offense intended to be punished." *United States v. Hinkle*, 637 F.2d 1154, 1157 (7th Cir. 1981).

Bates argues that the indictment fails to adequately set forth the elements of conversion because it does not charge that his handling of federaly guaranteed funds was in any way "unauthorized." Yet, the indictment alleges (1) that the school had a duty to refund unearned student loans to the lender within thirty to sixty days; (2) that

due to the participation agreement and the warnings of Acme's financial aid director, Bates knew of this duty; (3) that Bates specifically directed Acme personnel not to make refunds that were required by law; and (4) that Bates instead made management and salary payments to the Jacksons and to Education America, of which Bates happened to be vice president. These factual allegations clearly make out a charge that Bates's handling of Acme's federally guaranteed student loan funds was unauthorized.

Bates also contends, citing *Hinkle*, 637 F.2d at 1158, that the indictment is insufficient because the term "misapplication" is intrinsically vague. In *Hinkle*, we determined that an indictment charging use of a communication device to facilitate the commission of a felony involving a controlled substance, in violation of 21 U.S.C. § 843(b), was insufficient to inform the defendant of the nature of her alleged crimes. *Id.* Bates argues that "misapplication" is as uninformative as "facilitation." But Bates misunderstands the holding in *Hinkle*. The fatal ambiguity in *Hinkle* was that the indictment, although following the language of the statute in alleging the offense of facilitating a felony involving a controlled substance, failed to identify either the felony facilitated or the controlled substance involved. *Id.* The "facilitation" charge was duplicitous because it could have referred to any one of a number of criminal acts that the defendant may have committed.

Here, on the other hand, Bates has been charged with a distinct, identifiable offense: he willfully misapplied specified amounts of federally guaranteed Title IV funds on twelve specified occasions. Although admittedly bareboned, the indictment in this case included all of the requisite elements of willful misapplication under § 1097(a), and it certainly alleged sufficient facts to apprise Bates of the charges against him.

The judgment of the district court dismissing the indictment is VACATED, and the cause is REMANDED to the district court for further proceedings consistent with this opinion.

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

Date: September 20, 1996

(Caption Omitted)

The judgment of the District Court is VACATED, and this cause is REMANDED, in accordance with the decision of this court entered on this date.

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

October 23, 1996

(Caption Omitted)

The following are before the court:

1. MOTION FOR STAY OF MANDATE PENDING PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES SUPREME COURT, filed on October 9, 1996, by counsel for the appellee.

2. GOVERNMENT'S RESPONSE TO APPELLEE'S MOTION FOR STAY OF MANDATE PENDING PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES SUPREME COURT, filed on October 21, 1996.

IT IS ORDERED that #1 is GRANTED and the mandate is STAYED until December 19, 1996. If the appellant has filed a petition for a Writ of Certiorari by that date, the mandate shall remain stayed pending resolution of the proceedings before the Supreme Court. If he has failed to do so, the mandate shall issue forthwith. Counsel is reminded of his obligation to comply with Circuit Rule 41(e).

UNITED STATES SENATE

COMMITTEE ON LABOR AND HUMAN RESOURCES

Washington, DC 20510-6300

February 28, 1992

Mr. James B. Thomas, Jr.
Inspector General
United States Department of Education
400 Maryland Avenue, S.W.
Washington, D.C. 20202

Dear Mr. Thomas:

I am writing to make clear my intention in proposing a modification in the language of Section 490 of Title IV of the Higher Education Act. This modification is found in section 479 of S. 1150, the Senate version of legislation reauthorizing the Higher Education Act.

My proposal, which was adopted by the Committee on Labor and Human Resources and included in S. 1150 as approved by the full Senate, adds to Section 490 a specific reference to the failure to make refunds of federal loan and grant funds provided or insured under Title IV. My purpose in proposing this language was to clarify what is already intended by this section and to foreclose any argument that the section does not reach the failure to make refunds.

Section 490 of the Higher Education Act as currently written is extremely broad and reaches a variety of improper conduct involving Title IV funds. The knowing and willful failure to make refunds has properly been prosecuted as a misapplication of Title IV funds under this section. The language I proposed for inclusion in S. 1150 was never intended to imply in any manner that the current law did not reach such conduct. On the contrary, my intention was to facilitate prosecution of such

conduct by specifically referencing it. I made this proposal because it came to my attention during the reauthorization process that the failure of some school owners to make refunds or make timely refunds is, unfortunately, a widespread abuse that causes serious harm to the integrity of the federal student financial assistance programs and harm to the students the programs are meant to benefit.

It would be an unfortunate perversion of my intention if this clarifying language in S. 1150 concerning refunds were to be read as an indication that it is not a misapplication within the meaning of the current section 490 for a school owner knowingly and willfully to fail to make required refunds in connection with federally insured student loans and federal student grants.

Warmest regards,

/s/ Nancy
NANCY LANDON KASSEBAUM
United States Senator

SUPREME COURT OF THE UNITED STATES

No. 96-7185

GARRIT BATES,

Petitioner

v.

UNITED STATES

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

ON CONSIDERATION of the motion for leave to proceed herein in forma pauperis and of the petition for writ of certiorari, it is ordered by this Court that the motion to proceed in forma pauperis be, and the same is hereby, granted; and that the petition for writ of certiorari be, and the same is hereby, granted.

February 18, 1997

Supreme Court, U.S.
FILED
APR 25 1997
OFFICE OF THE CLERK

(5)

No. 96-7185

IN THE
Supreme Court of the United States
OCTOBER TERM, 1996

GARRIT BATES,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

---

BRIEF FOR THE PETITIONER

C. RICHARD OREN
(Appointed by this Court)
1104 Main Street
P.O. Box 532
Rochester, Indiana 46975
(219) 223-9485
Attorney for Petitioner

27 pp

QUESTION PRESENTED

Must the United States of America prove fraudulent intent on the part of the defendant, Garrit Bates, as an essential element of the crime of knowingly and willfully misapplying federally insured funds, proscribed by 20 U.S.C. § 1097(a)?

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
TABLE OF AUTHORITIES	v
OPINIONS BELOW	1
JURISDICTION STATEMENT	1
STATUTORY PROVISION INVOLVED	1
STATEMENT OF THE CASE	1
A. Factual Background	1
B. Procedural History	2
SUMMARY OF THE ARGUMENT	3
ARGUMENT	6
I. MR. BATES MAINTAINS THAT THE INDICTMENT BY WHICH HE WAS CHARGED WITH VIOLATIONS OF 20 U.S.C. § 1097(a) IS DEFICIENT ON ITS FACE AND SHOULD BE DISMISSED	6
II. THE LANGUAGE OF 20 U.S.C. § 1097(a) INDICATES THE INTENT OF CONGRESS THAT THE OFFENSE OF MISAPPLICATION OF FUNDS CONTAIN THE ESSENTIAL ELEMENT OF SPECIFIC INTENT	8
III. THE INTENT OF CONGRESS IS FULFILLED BY A DEFINITION OF "MISAPPLIES" UNDER 20 U.S.C. § 1097(a) WHICH INCLUDES THE ESSENTIAL ELEMENT OF FRAUDULENT INTENT	11

TABLE OF CONTENTS—Continued

	Page
IV. THE VIEW THAT CONGRESS UNDERSTANDS THE DEFINITION OF "MISAPPLY" IN 20 U.S.C. § 1097(a) TO CONTAIN THE ESSENTIAL ELEMENT OF FRAUDULENT INTENT IS ALSO SUPPORTED BY CONGRESS' 1992 AMENDMENT OF THE STATUTE AND REGULATIONS	13
V. APPLICATION OF THE RULE OF LENITY RESOLVES ANY POTENTIAL AMBIGUITY IN THE DEFINITION OF "KNOWINGLY AND WILLFULLY MISAPPLIES" TO INCLUDE THE ESSENTIAL ELEMENT OF FRAUDULENT INTENT	16
VI. THE INDICTMENT FAILS TO ALLEGE FACTS SUFFICIENT TO INFER THAT MR. BATES CONVERTED FUNDS WITH THE INTENT TO DEFRAUD; NOR, DO THE WORDS OF THE STATUTE UNAMBIGUOUSLY SET FORTH THE ESSENTIAL ELEMENTS OF THE OFFENSE CHARGED PURSUANT TO 20 U.S.C. § 1097(a)	17
CONCLUSION	21

TABLE OF AUTHORITIES

Cases:	Page
United States Supreme Court	
Albernaz v. United States, 450 U.S. 333 (1981)	16
Connecticut National Bank v. Germain, 503 U.S. 249	8
Consumer Product Safety Commission v. GTE Sylvania, Inc., 447 U.S. 102	8
Hagner v. United States, 285 U.S. 427 (1932)	6
Hamling v. United States, 418 U.S. 87 (1974)	7, 17, 20
Liparota v. United States, 471 U.S. 419 (1985)	16
Morissette v. United States, 342 U.S. 246 (1952)	4, 9, 10 17
Ratzlaf v. United States, 510 U.S. 135	9
Securities Industry Association v. Board of Governors of the Federal Reserve System, 468 U.S. 137 (1984)	11
Staples v. United States, 511 U.S. 600, 114 S.Ct. 1793	8
United States v. Bailey, 444 U.S. 394 (1980)	9
United States v. Bass, 404 U.S. 348, 92 S.Ct. 523	16
United States v. Britton, 107 U.S. 655 (1983)	12
United States v. Carll, 105 U.S. 611, 26 L.Ed. 1135 (1882)	7
United States v. Freed, 401 U.S. 601 (1971)	10
United States v. Thompson/Center Arms Company, 504 U.S. 505 (1992)	16
United States v. X-Citement Video, 115 S.Ct. 464 (1994)	12
United States v. Wells, 119 S.Ct. 921	9
United States Court of Appeals	
United States v. Bates, 96 Fed.3d 964 (C.A. 7th 1996)	11
United States v. Brown, 742 Fed.2d 363 (C.A. 7th 1984)	12
United States v. Kammer, 1 Fed.3d 1161 (C.A. 11th 1993)	7, 12

TABLE OF AUTHORITIES—Continued

	Page
United States District Court	
United States of America v. Garrit Bates, Memorandum and Order of United States District Court for the Northern District of Indiana, [Pet. App., pp. A-14 to A-23]	12
United States v. Jakeway, 783 F.Supp. 590 (M.D. Fla. 1992)	12
United States Statutes	
Fed. R. Crim. Proc. 7(c) (1)	6
Code of Federal Regulations	
34 C.F.R. § 682.604(d) (1) (ii) (B)	14

OPINIONS BELOW

The Opinion of the United States Court of Appeals for the Seventh Circuit is reported at 96 Fed. 3d 964 and is set forth in its entirety as Petitioner's Appendix A, pages A-1 through A-13, to the Petition for Writ of Certiorari.

The Memorandum and Order of the District Court is unreported, but is set forth in its entirety as Petitioner's Appendix B, pages A-14 through A-23 to the Petition for Writ of Certiorari.

JURISDICTION STATEMENT

The Court of Appeals entered its judgement on September 20, 1996. The Petition for Writ of Certiorari was filed on December 23, 1996, and was granted on February 18, 1997. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISION INVOLVED

20 U.S.C. § 1097(a) provided, prior to its amendment in 1992, that:

> Any person who knowingly and willfully embezzles, misapplies, steals, or obtains by fraud, false statement, or forgery any funds, assets, or property provided or insured under the subchapter and part C of subchapter I of Chapter 34 of Title 42 shall be fined not more than $10,000 or imprisoned for not more than Five (5) years, or both; but if the amount so embezzled, misapplied, stolen, or obtained by fraud, false statement, or forgery does not exceed $200, the fine shall not be more than $1,000 and imprisonment shall not exceed One (1) year, or both.

STATEMENT OF THE CASE

A. Factual Background

Mr. Garrit (Jerry) Bates, began employment with Education America, Inc., in January of 1986. Education America, Inc., operated vocational and technical schools

located in Indiana and Wisconsin. Mr. Bates held the nominal title of vice-president of Education America, Inc., with his primary responsibility being overseeing student recruitment at various schools. Mr. Bates had no ownership interest in Education America, Inc.

In late 1988 or early 1989, Education America, Inc. realized that Acme Institute of Technology, located in South Bend, Indiana, ("Acme") was experiencing financial difficulty. As a result of this difficulty, Mr. Bates was given the additional responsibility in 1989 of determining which bills of Acme's were to be paid first, in an effort to steer the school through the financially troubled times. Ultimately, the efforts of Mr. Bates and others involved at Acme and Education America, Inc., were unsuccessful in resuscitating the financial health of the school, with Acme ceasing operations on June 5, 1990. At the time it ceased operations, Acme had unpaid refund liability under the guaranteed student loan program which was substantial.

In January 1991, Mr. Bates began employment with the Indiana Public Employees Retirement Fund where he presently remains employed. Mr. Bates voluntarily cooperated with the investigation of the Department of Education into the refund liability of Acme throughout the calendar year of 1992.

B. Procedural History

Mr. Bates was indicted by a federal grand jury on September 8, 1994. The indictment charged Mr. Bates with knowingly and willfully misapplying specified amounts of federally guaranteed student loan funds on twelve (12) separate occasions between January 15 and June 15, 1990, in violation of 20 U.S.C. § 1097(a) and 18 U.S.C. § 2. Mr. Bates moved to dismiss the indictment on February 7, 1995. Mr. Bates contended that the indictment did not reveal any allegd facts which would

support a conclusion that Mr. Bates had converted any funds guaranteed or furnished by the United States; and, that the indictment failed to allege that Mr. Bates intended to fraudulently convert funds guaranteed or owned by the United States Department of Education.

On April 17, 1995, the United States District Court entered its memorandum and order dismissing the indictment, agreeing with Mr. Bates that the indictment had failed to allege fraudulent intent on the part of Mr. Bates as an essential element of the crime. Specifically, the District Court found that the indictment was insufficient on its face in that each count of the indictment failed to state that Mr. Bates misapplied protected funds "with an intent to injure or defraud the United States."

On May 17, 1995, United States of America filed its notice of appeal. After submission of briefs, the matter was argued on February 12, 1996, before the United States Court of Appeals for the Seventh Circuit. The opinion of the Seventh Circuit was issued on September 20, 1996, reversing the United States District Court by vacating the judgment of the Court dismissing the indictment and reinstating the prosecution. In so doing, the United States Court of Appeals found that the specific intent of a defendant to injure or defraud the United States is not an element of the offense charged.

SUMMARY OF ARGUMENT

Mr. Bates is challenging the sufficiency of the indictment charging him with the offense of knowing and willfully misapplying funds in violation of 20 U.S.C. § 1097 (a). Specifically, Mr. Bates contends that the indictment did not set forth the essential elements of the offense charged, to-wit: (1) conversion of funds to his use or the use of another with (2) intent to defraud. Since the government has conceded, and the courts below have agreed, that conversion is an essential element of the offense, the central issue before the Court is whether or not

fraudulent intent is an essential element of criminal misapplication of funds as proscribed by § 1097(a).

Mr. Bates first argues that the plain language of the statute indicates the intent of Congress that specific intent is an element of the offense. Without question the phrase "knowingly and willfully" modifies the offenses of "embezzle," "misapply" and "steal" set forth in the statute. The term "knowingly" is often used to indicate a state of mind which harbors general intent. Here Congress has also used the term "willfully" in addition to "knowingly" in reference to the prohibited conduct. Since "willfully" should not be viewed as surplusage, the use of the phrase "knowingly and willfully" indicates the intent of Congress that the highest degree of mental culpability, specific intent, is an essential element of these offenses. In addition, the criminal sanctions of the Higher Education Act of 1965 embodied in § 1097(a) were enacted in 1980, twenty-eight (28) years following this Court's decision in *Morissette v. United States*. In *Morissette*, this Court found that statutory offenses which were variants of the common law crime of larceny were presumed to have retained the concept of mens rea as an element of the offense in the absence of express intent to the contrary. Congress is presumed to know the import of Supreme Court precedent in enacting statutes. The offense of "misapply" is found in a list of offenses which are variants of the common law crime of larceny and should therefore be presumed similar; these factors bolster the conclusion that the language of the statute indicates Congressional intent that "misapplication" include the element of specific intent.

Mr. Bates next argues that a definition of "misapplies" which includes the essential element of fraudulent intent fulfills the intent of Congres that the highest degree of mental culpability apply to the offenses of "embezzlement," "misapplication," and "stealing" under § 1097(a). In general usage the term misapplication is intrinsically vague in that it could emcompass a variety of acts. However the government has conceded, and the courts below agree that a type of conduct, (conversion) is an element of "criminal misapplication." The purpose of scienter is to disinguish innocent conduct from criminal conduct. By including fraudulent intent as an essential element of criminal misapplication of funds, the otherwest innocent conduct of maladministration of a business enterprise through unwise use of funds can be distinguished from criminal misapplication.

Mr. Bates further argues that the 1992 Amendment of § 1097(a) also supports this conclusion. This amendment criminalized the specific conduct "fail to refund" which is a possible result of the wrongful use, or misapplication of funds. This amendment constitutes a tacit acknowledgement by Congress that the offense of misapplication focuses on the use of the funds. Prior to 1992, the regulatory scheme did not sufficiently restrict the *use* of the funds at issue which apparently aliowed unwise use of these funds *without* fraudulent intent (i.e. maladministration) to proliferate and adversely affect student financial aid programs. The fact that this problem was addressed in Congress by specifically criminalizing the act of failing to make refunds and not merely by promulgation of regulations which would have provided more ways for an "unauthorized use" to be proven, reinforces the conclusion that Congress considered a § 1097(a) "misapplication" to include the element of fraudulent intent.

Mr. Bates also argues that the rule of lenity would support a reading of the statute requiring fraudulent intent as an essential element of the offense of misapplication of funds should the intent of Congress be found ambiguous. This would yield a less harsh result than any alternative reading posited by the government in the courts below and would not expand the reach of this statutory crime in the absence of clear Congressional intent to do so.

Having established that the essential elements of criminal misapplication of funds are conversion and fraudulent intent, Mr. Bates demonstrates that a critical examination of the indictment does not reveal facts supporting *either* of the essential elements of the offense because there are no specific allegations as to how the funds in question were actually used. Further, although the individual counts of the indictment are set forth in the words of the statute, they are not free of uncertainty and ambiguity. Because of these failings, the indictment is deficient on its face and should be dismissed.

ARGUMENT

I. MR. BATES MAINTAINS THAT THE INDICTMENT BY WHICH HE WAS CHARGED WITH VIOLATIONS OF 20 U.S.C. § 1097(a) IS DEFICIENT ON ITS FACE AND SHOULD BE DISMISSED.

Mr. Bates is challenging the sufficiency of the indictment. An, ". . . indictment . . . shall be a plain, concise and definite written statement of the essential facts constituting the offense charged." Fed. R. Crim. Proc. 7(c)(1). It has long been understood that an indictment must be more strictly examined for sufficiency if challenged prior to the rendering of a verdict on the merits of the case. *See, Hagner v. United States,* 285 U.S. 427 (1932). This case finds itself before the Court as a result of the granting of a motion to dismiss by the United States DistrictCourt for the Northern District of Indiana prior to commencement of trial, a subsequent reversal by the United States Court of Appeals for the Seventh Circuit and grant of Writ of Certiorari by this Court. Under these circumstances a strict review of the indictment should apply.

This Court has succintly stated its standard for determining the sufficiency of an indictment as follows:

> Our prior cases indicate that an indictment is sufficient if it, first, contains the elements of the offense charged and fairly informs the defendant of the charge against which he must defend, and, second, enables him to plead an acquittal or conviction in bar of future prosecutions for the same offense. . . . [citations omitted] . . . it is generally sufficient that an indictment set forth the offense in the words of the statute itself, as long as "those words of themselves fully, directly and expressly, without any uncertainty or ambiguity, set forth all the elements necessary to constitute the offense intended to be punished." *United States v. Carll,* 105 U.S. 611, 612, 26 L.Ed. 1135 (1882).

Hamling v. United States, 418 U.S. 87, 117 (1974).

Mr. Bates contends that the indictment at issue in this case does not meet the foregoing standard.

To properly resolve the case before the Court, the essential elements of the offense of "knowingly and willfully misapplying funds provided an insured under subchapter IV chapter 28 of Title 20 of the United States Code", must be identified. Mr. Bates asserts that the definition of a criminal misapplication of funds includes: (1) a conversion of property to the use of the defendant or a third party, and, (2) fraudulent intent. *See, United States v. Kammer,* 1 Fed. 3d 1161, 1165 (C.A. 11th, 1993). Mr. Bates submits that for the indictment to have sufficiently apprised him of the charges asserted by the government, in addition to the introductory factual allegations, the portion of the indictment charging each count should, at a minimum, read as follows:

> On or about [*a given date*], in the Northern District of Indiana, Garrit Bates, a/k/a Jerry Bates, defendant herein, did knowingly and willfully misapply funds, to wit: [*dollar amount*], provided an insured under subchapter IV of chapter 28 of Title 20 of the United States Code *by converting said funds to his use or the use of another with the intent to defraud.*

II. THE LANGUAGE OF 20 U.S.C. § 1097(a) INDICATES THE INTENT OF CONGRESS THAT THE OFFENSE OF MISAPPLICATION OF FUNDS CONTAIN THE ESSENTIAL ELEMENT OF SPECIFIC INTENT.

Resolution of the issue presented in this case presents a problem of statutory construction. The starting point of an inquiry into statutory construction is the language of the statute itself. *Staples v. United States*, 511 U.S. 600, 114 S.Ct. 1793, 1796, citing *Connecticut National Bank v. Germain*, 503 U.S. 249. In the absence of a clearly expressed legislative intention to the contrary, the language of the statute itself must ordinarily be regarded as conclusive. *Consumer Product Safety Commission v. GTE Sylvania, Inc.*, 447 U.S. 102, 108.

The statute at issue defines a federal offense for "[a]ny person who knowingly and willingly embezzles, misapplies, steals, or obtains by fraud, false statement or forgery any funds, assets, or property provided or insured under the subchapter and part C of subchapter I of chapter 34 of Title 42 . . .". Specifically, Mr. Bates was charged in a twelve (12) count indictment that he "did knowingly and willingly misapply funds . . ., provided and insured under subchapter IV of chapter 28 of Title 20 of the United States Code." [J.A. pp. 6-17].

The government, arguing in the courts below, has maintained that the definition of "misapplication" of funds under § 1097(a) is simply "conversion of funds to the defendant's own use, or the use of others". Obviously, the main disagreement between Mr. Bates and the Government is whether or not fraudulent intent is an essential element of the offense of misapplication of funds under § 1097(a).

This Court is often called upon to determine the existence or non-existence of scienter as an element of offenses created by statute where Congress has not included specific

language in the statute as indicia of its intent. However, such is not the case in construing the offense of "misapplication" proscribed by 20 U.S.C. § 1097(a), as Congress has stated that to commit the offense the actor must engage in the prohibited conduct "knowingly and willfully".

Here, Congress has specifically employed the term "knowingly" in reference to the prohibited conduct. "Knowingly" has been found to indicate, at the very least, a state of mind encompassing a low degree culpability roughly synonymous with general intent at common law. See, *United States v. Bailey*, 444 U.S. 394 (1980). However, in addition to "knowingly," Congress has also employed the term "willfully" to describe the state of mind necessary to constitute prohibited conduct within the ambit of § 1097(a). This Court is hesitant to view a statutory term as surplusage, or as having no consequence. See, *Ratzlaf v. United States*, 510 U.S. 135, 140. In fact, this Court ". . . presumes that each term in a criminal statute carries meaning." *United States v. Wells*, 119 S. Ct. 921, 929. If "willfully" is not considered surplusage and given meaning, a conclusion is supported that Congress intended (by requiring willful conduct in addition to knowing conduct) that the highest degree of mental culpability (specific intent) be required to establish the offenses of "embezzlement," "misapplication" or "stealing" under § 1097(a).

This Court also ". . . presume[s] that Congress expects its statutes to be read in conformity with this Court's precedents. . . ." *Wells*, at 929. The Higher Education Act of 1965 of which 20 U.S.C. § 1097(a) is a part, was enacted some thirteen (13) years subsequent to this Court's landmark decision in *Morissette v. United States*, 342 U.S. 246 (1952), with the criminal provisions of § 1097(a) being enacted in 1980. In *Morissette*, this Court engaged in a lengthy and insightful analysis of the importance of scienter in defining criminality under the common law. Because of the importance of mens rea or

scienter as elements of common law crimes, this Court found that, in the absence of specific congressional intent to the contrary, the mere lack of language indicating a mens rea requirement did not necessarily mean that this element of the offense had been abandoned by Congress. Against that backdrop, the Court held that criminal intent is an essential element of the crime of "knowing conversion" of property of the United States in violation of 18 U.S.C. § 641. In reaching this conclusion this Court noted that:

> Stealing, larceny, and its variants and equivalents, were among the earliest offenses known to the law that existed before legislation; they are invasions of rights of property which stir a sense of insecurity in the whole community and arouse public demand for retribution, the penalty is high and, when a sufficient amount is involved, the infamy is that of a felony, which, says *Maitland* is . . . as bad a word as you can give to man or thing.

Morissette at p. 260.

It is important to note that in § 1097(a) the offense of "misapplication" is sandwiched between the offenses of "stealing" (one of the earliest offenses known to the law) and "embezzlement," a variant of larceny, which was ". . . borrowed from the common law where scienter was historically required . . .". *United States v. Freed*, 401 U.S. 601, 607 (1971). Since Congress is presumed to have been aware of the view of this Court (as expressed in *Morissette*) that scienter is an essential element of the variant forms of the common law crime of larceny, the inclusion of "misapplication" in a list of these variant offenses would infer that Congress considered all of these offenses to be similar. As this Court has observed, a ". . . familiar principle of statutory construction is that words grouped in a list should be given related meaning." *Securities Industry Association v. Board of Governors of*

the Federal Reserve System, 468 U.S. 137, 167 (1984). Accordingly, support is given to a conclusion that the plain language of the statute indicates Congressional intent that the prohibited offenses, including "misapplication," be committed with specific intent on the part of a defendant.

III. THE INTENT OF CONGRESS IS FULFILLED BY A DEFINITION OF "MISAPPLIES" UNDER 20 U.S.C. § 1097(a) WHICH INCLUDES THE ESSENTIAL ELEMENT OF FRAUDULENT INTENT.

It is quite clear, and the government has never contended otherwise, that the phrase, "knowingly and willfully" modifies the terms "misapplies" and "steals" as well as "embezzles," set forth in § 1097(a). Since Congress intended (by proscribing "knowing and willfull" conduct) to require proof of the highest degree of mental culpability for each of these offenses (e.g. specific intent), one must next examine the impact of this requirement upon the specific offense of misapplication of funds which was alleged by the government to have been violated by Mr. Bates.

In performing this analysis, it seems logical that the first step would be to identify the specific acts or type of conduct encompassed by the term "misapplication." An ordinary or common sense understanding of the term is vague, in that many different acts could conceivably constitute "misapplication" in general usage. Indeed, the "legal definition" of misapplication supplied by Black's Law Dictionary, Revised Fourth Edition, adds very little definiteness of understanding to the term by defining "misapplication" as follows: "Improper, illegal, wrongful, or corrupt use or application of funds, property, etc." However, many courts, including the courts below, are in agreement that a certain type of conduct, that is, conversion, is an element of the offense of criminal misapplication as proscribed by § 1097(a). See, *United States v. Bates*, 96 Fed. 3d 964 (C.A. 7th, 1996); *United States v.*

Kammer, 1 Fed. 3d 1161 (C.A. 11th, 1993); *United States v. Brown*, 742 Fed. 2d 363 (C.A. 7th, 1984); *United States v. Jakeway*, 783 F. Supp. 590 (M.D. Fla. 1992); *United States of America v. Garrit Bates, Memorandum and Order of United States District Court for the Northern District of Indiana*. [Pet. App., pp. A-14 to A-23]. Even the government, in the instant case, conceded that conversion was an element of the offense of misapplication of funds under § 1097(a). [Pet. App. p. A-7].

The underlying purpose of a scienter requirement is to separate innocent conduct from criminal behavior. "Criminal intent serves to separate those who understand the wrongful nature of their act from those who do not, but does not require knowledge of the precise consequences that may flow from that act once aware that the act is wrongful." *United States v. X-Citement Video*, 115 S. Ct. 464, 469 n.3 (1994). In the very real circumstances presented in this case, the scienter requirement would serve to distinguish between criminal misapplication of funds and mere maladministration of a business enterprise which failed. See, *United States v. Britton*, 107 U.S. 655, 667 (1883). The purpose of Congress in requiring that the highest degree of mental culpability apply to criminal misapplication under § 1097(a) must surely have been to ensure that criminal sanctions were not applied to those individuals who committed acts of poor judgement or negligence which may merely form the basis for a civil remedy. This Court recently pronounced that the "scienter requirement should apply to each of the statutory elements which criminalize otherwise innocent conduct." *X-Citement Video*, p. 469. Where the only overt act of a defendant which may be offered to prove the offense of criminal misapplication is that the defendant exercised dominion or control over the property of another to his benefit or the benefit of a third party, the factor which would separate otherwise innocent conduct from criminal

activity would be whether or not the defendant intended by his conduct to defraud.

The inclusion of fraudulent intent as an essential element of criminal misapplication under § 1097(a), therefore, satisfies the congressional intent that the crime contain the highest degree of mental culpability.

IV. THE VIEW THAT CONGRESS UNDERSTANDS THE DEFINITION OF "MISAPPLY" IN 20 U.S.C. § 1097(a) TO CONTAIN THE ESSENTIAL ELEMENT OF FRAUDULENT INTENT IS ALSO SUPPORTED BY CONGRESS' 1992 AMENDMENT OF THE STATUTE AND REGULATIONS.

Mr. Bates was indicted for conduct which allegedly occurred in 1990. The allegations of misconduct against Mr. Bates are not unambiguously stated; they possibly consist of twelve (12) instances where refunds due insured lenders under the guaranteed student loan program were not made.

In 1992, Congress amended 20 U.S.C. § 1097(a) to read:

> Any person who knowingly and willfully embezzles, misapplies, steals, obtains by fraud, false statement or forgery, or fails to refund, any funds, assets or property provided or insured under the subchapter and part C of subchapter I of chapter 34 of Title 42 or attempts to so embezzle or misapply, steal, obtain by fraud, false statement or forgery or fail to refund any funds, assets or property shall be fined not more than $20,000.00 or imprisoned for not more than 5 years or both except if the amount so embezzled, misapplied, stolen, obtained by fraud, false statement, or forgery, or failed to be refunded does not exceed $200.00, then the fine shall not be more than $5,000.00 and imprisonment shall not exceed 1 year or both.

The 1992 Amendment of § 1097(a) by Congress seemingly was intended to impose new duties upon schools and

clarify the potential criminal liability of those entities who fail to make refunds. This concept is supported by the fact that the Department of Education promulgated amendments to its regulations, subsequent to the 1992 amendment to the statute, which significantly affected the manner in which a school must process and apply a student borrower's loan proceeds. These regulations specifically address the obligation of the school regarding loan proceeds which a student requests in writing be retained by the school so as to assist the student in managing his or her loan funds for the remainder of the academic year. As of July 1, 1993, 34 C.F.R. § 682.604(d)(1)(ii)(B) mandated, in pertinent part, that: "The school shall deposit these funds in a designated trust account and may not commingle them with other funds or use them for any other purpose." Prior to the addition of this language, a participating school was permitted to commingle unearned student loan funds with other funds which were used in the operation of the institution,—as the government alleges was done by Acme.

Even though Acme and other participating schools were allowed to commingle these funds, Mr. Bates acknowledges that the legislative history of 20 U.S.C. § 1097(a) does indicate that the language of § 1097(a) was broad enough to include prosecuting the failure to make refunds as a result of a criminal misapplication of funds. That this was the intent of Congress was clearly set forth by United States Senator Landen Kassenbaum in her correspondence of February 28, 1992, to Mr. James B. Thomas, Jr., Inspector General of the United States Department of Education. [J.A. p. 24]. Senator Kassenbaum was a sponsor of the legislation which amended § 1097(a) in 1992. Senator Kassenbaum explains that Congress understood its original intent to be that a knowing and willful failure to make refunds could appropriately be prosecuted as a misapplication of Title IV funds, but it was her intent and the intent of Congress through the 1992 amendment to

facilitate prosecution of such conduct by specifically referencing it in the statute.

Mr. Bates submits that the mere fact that a failure to make refunds could properly be prosecuted as the result of a knowing and willful misapplication of funds does not mean that, prior to July 23, 1992, the failure to timely make refunds, *in and of itself* constituted a criminal violation of 20 U.S.C. § 1097(a). In 1992, Congress made the prosecution of this conduct easier by specifically proscribing the conduct of failing to make refunds, thereby eliminating the necessity to show that there was a "misapplication" which resulted in a failure to make refunds. This manner of amending the statute constitutes a tacit acknowledgement by Congress that the offense of "misapplication" focuses on the manner in which the funds were used. A regulatory scheme which, prior to 1992, did not stringently restrict the use of student loan proceeds by a school, combined with a statutory offense which required misuse of funds with fraudulent intent, apparently allowed innocent conduct which constituted maladministration to proliferate and adversely impact student financial aid programs. The fact that Congress addressed this concern by creating the particularized offense of "fails to refund" and by the promulgation of more stringent regulations reinforces the conclusion that Congress knew misapplication under § 1097(a) contained the essential element of intent to defraud. Had fraudulent intent not been an element of "misapplication" promulgation of regulations severely restricting the use of funds could have addressed the problem by merely providing more ways to prove an "unauthorized use" of funds.

V. APPLICATION OF THE RULE OF LENITY RESOLVES ANY POTENTIAL AMBIGUITY IN THE DEFINITION OF "KNOWINGLY AND WILLFULLY MISAPPLIES" TO INCLUDE THE ESSENTIAL ELEMENT OF FRAUDULENT INTENT.

It is conceivable that the government will argue that the intent of Congress is not clear and that the statute in question is susceptible of another reasonable reading regarding whether or not fraudulent intent is an essential element of the offense of knowing and willful misapplication of funds in violation of 20 U.S.C. § 1097(a). If such is the case, Mr. Bates submits that any such ambiguity would be resolved in his favor by application of the rule of lenity. This Court has recognized that the ". . . 'touchstone' of the rule of lenity 'is statutory ambiguity'. . . . lenity thus serves only as an aid for resolving an ambiguity; it is not to be used to beget one." *Albernaz v. United States*, 450 U.S. 333, 342 (1981). See, also, *United States v. Thompson/Center Arms Company*, 504 U.S. 505 (1992).

Generally, the rule of lenity means that courts will adopt the less harsh meaning of a statute where the intent of Congress is ambiguous. See, Black's Law Dictionary, Fourth Edition.

> Application of the rule of lenity ensures that criminal statutes will provide fair warning concerning conduct rendered illegal and strike the appropriate balance between the legislature, the prosecutor and the court in defining criminal liability. See, *United States v. Bass, supra,* 404 U.S., at 348, 92 S.Ct., at 523 ('[B]ecause of the seriousness of criminal penalties, and because criminal punishment usually represents the moral condemnation of the community, legislatures and not courts should define criminal activity')."

Liparota v. United States, 471 U.S. 419, 427 (1985).

This Court has also acknowledged that ". . . the doctrine which denies to the federal judiciary power to

create crimes forthrightly admonishes that we should not enlarge the reach of enacted crimes by constituting them from anything less than the incriminating components contemplated by the words used in the statute." *Morissette v. United States*, 342 U.S. 246, 263 (1952).

In the case at hand, a reading of 20 U.S.C. § 1097(a) which would require proof of fraudulent intent as an essential element of the crime of knowingly and willfully misapplying federally insured funds would be less harsh than any alternative reading of this statute proposed by the government in the courts below. Further, such a reading would ensure that the judiciary did not enlarge the reach of this statutory crime without a clear statement from Congress that criminal intent was not an essential element of said crime.

Application of the rule of lenity, if appropriate, supports Mr. Bates' position in this case that fraudulent intent is an essential element of "knowing and willful misapplication" of funds in violation of § 1097(a).

VI. THE INDICTMENT FAILS TO ALLEGE FACTS SUFFICIENT TO INFER THAT MR. BATES CONVERTED FUNDS WITH THE INTENT TO DEFRAUD; NOR, DO THE WORDS OF THE STATUTE UNAMBIGUOUSLY SET FORTH THE ESSENTIAL ELEMENTS OF THE OFFENSE CHARGED PURSUANT TO 20 U.S.C. § 1097(a).

Having established in the preceding sections that the offense of "knowingly and willfully misapplying" funds as proscribed by 20 U.S.C. § 1097(a) contains the essential elements of (1) conversion, and, (2) fraudulent intent, it must now be determined whether the indictment is sufficient under the standards set forth in *Hamling*.

The factual allegations of the indictment do not contain any facts from which it could be inferred that Mr. Bates either *converted* or harbored any *intent to defraud* anyone

by the alleged acts. Scrutiny of the sixteen (16) introductory paragraphs of the indictment reveal only the following *vis-a-vis* Mr. Bates' status or actions, or the actions of any person with whom he was associated: (a) that Mr. Bates was treasurer of the Board of Trustees of Acme, [J.A. p. 2; indictment, paragraph 1]; (b) that Mr. Bates was vice-president of Education America, a for-profit corporation, [J.A. p. 2; indictment, paragraph 2]; (c) that James W. Jackson, the president of Acme had signed a program participation agreement with the Department of Education on behalf of Acme, and that Mr. Bates did sign a program participation agreement on behalf of another school operated by Education America, [J.A. p. 3; indictment, paragraph 5]; (d) that the decisions of James W. Jackson and Laurenda Jackson as well as Mr. Bates resulted in the failure of Acme to pay refunds which were due lending institutions under the guaranteed student loan program in which Acme participated, [J.A. p. 4; indictment, paragraph 6]; (e) that Mr. Jackson had corresponded with the director of Acme and the director of Interstate Technical Institute, located in Ft. Wayne, Indiana, instructing the schools to remit a ten (10%) percent management fee to Education America, and a regular salary for James and Laurenda Jackson on a monthly basis, and that Mr. Bates had oversight authority at Interstate Technical Institute, [J.A. p. 4; indictment, paragraph 7]; (f) that Education America discontinued the use of a special bank account which segregated unearned income from the general account of Acme, [J.A. pp. 4-5; indictment, paragraph 9]; (g) that in early 1989, Mr. Bates began determining which bills would or would not be paid with the understanding that payments to Mr. and Mrs. Jackson and Education America and other bills took priority over payments of refunds; and, that Mr. Bates specifically instructed Acme employees not to make student loan refunds, [J.A. p. 5; indictment, paragraph 11]; (h) Mr. Bates released the financial aid director of Acme from

all responsibility concerning refunds on guaranteed student loans, at her request. However, the financial aid director was advised to continue to prepare refund documents to be approved by the corporation for payment, [J.A. p. 5; indictment, paragraph 12]; (i) and, when Acme ceased operations on or about June 5, 1990, unrefunded, unearned income from the guaranteed student loan program had accrued to a total amount of One-Hundred Thirty-nine Thousand Six Hundred Forty-nine and No/100 ($139,649.00) Dollars during the period that Mr. Bates acted as the chief financial officer of Acme, [J.A p. 6; indictment, paragraph 15-16].

A careful reading of the factual allegations of the indictment reveals that it does not state how student loan proceeds were *actually used* by Acme during the period that Mr. Bates was making day-to-day decisions on payment of financial obligations of Acme. Since there is no specific statement regarding the actual use of these funds, it is impossible to make a determination as to whether or not any such use was in fact allowed under the civil regulations. This omission by the government is especially important in light of the fact that no Department of Education regulations prohibited commingling of student loan funds with other operating funds of a school in 1989 and 1990. The factual allegations of the indictment simply do not support a conclusion that a conversion is being charged as an essential element of the offense.

Similarly, the factual allegations of the indictment do not support an inference that Mr. Bates harbored an intent to defraud anyone as the second essential element of the offense of knowingly and willfully misapplying funds. Without knowing how the funds in questions *were actually used* it is simply impossible to infer an intent to defraud from Mr. Bates alleged conduct. The factual allegations simply do not state the essential element of fraudulent intent.

The portion of the indictment setting forth the twelve (12) specific counts of violation of 20 U.S.C. § 1097(a) merely describe the offense in the words of the statute itself. Therefore, it must be determined whether or not the words of the statute "fully, directly, and expressly, without any certainty or ambiguity, set forth all of the elements necessary to constitute the offense intended to be punished." See, *Hamling, supra* p. 117. Mr. Bates submits that they do not, as to either essential element of the offense. As pointed out hereinabove, the word "misapplication" is intrinsically vague since a variety of acts or conduct could, under appropriate circumstances, be considered misapplication. Something more definite must be stated to give a defendant enough information to defend the allegations. An explanatory phrase describing the conduct complained of by the government which falls within the ambit of "misapplication" is necessary to apprise the defendant that an essential element of offense is conversion.

Further, the phrase "knowingly and willfully," in the absence of precedent on the precise issue, is ambiguous, as it can be taken to mean simply that a defendant intentionally did some act. Thus, the specific counts of the indictment also harbor uncertainty as to whether or not the government must prove fraudulent intent as an essential element of the crime.

Because of these uncertainties and because the factual allegations do not specifically inform the defendant as to how the funds in question were *actually used*, the indictment does not meet the standard set forth in *Hamling* and is defective on its face.

CONCLUSION

For the foregoing reasons, the judgement of the United States Court of Appeals for the 7th Circuit should be vacated and the indictment of Mr. Bates dismissed.

Respectfully submitted,

C. RICHARD OREN
(Appointed by this Court)
1104 Main Street
P.O. Box 532
Rochester, Indiana 46975
(219) 223-9485
Attorney for Petitioner

Supreme Court, U.S.
FILED
JUN 13 1997
CLERK

No. 96-7185

In the Supreme Court of the United States

OCTOBER TERM, 1996

GARRIT BATES, PETITIONER

v.

UNITED STATES OF AMERICA

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES

WALTER DELLINGER
Acting Solicitor General
JOHN C. KEENEY
Acting Assistant Attorney General
MICHAEL R. DREEBEN
Deputy Solicitor General
LISA SCHIAVO BLATT
Assistant to the Solicitor General
DANIEL S. GOODMAN
Attorney
Department of Justice
Washington, D.C. 20530-0001
(202) 514-2217

44 pp

QUESTION PRESENTED

Whether intent to injure or defraud the government is an element of the offense of knowingly and willfully misapplying federal student loan funds, in violation of 20 U.S.C. 1097(a).

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Statutory provision involved	1
Statement	2
Summary of argument	10
Argument:	
A. "Intent to injure or defraud" is not an element of the offense defined by 20 U.S.C. 1097(a)	12
B. The indictment sufficiently alleges the offense of misapplication under Section 1097(a)	31
Conclusion	34
Appendix	1a

TABLE OF AUTHORITIES

Cases:

Browder v. *United States*, 312 U.S. 335 (1941)	18, 19
Cheek v. *United States*, 498 U.S. 192 (1991)	21, 22
Fogerty v. *Fantasy, Inc.*, 510 U.S. 517 (1994)	30
Garrett v. *United States*, 396 F.2d 489 (5th Cir.), cert. denied, 393 U.S. 952 (1968)	27
Golden v. *United States*, 318 F.2d 357 (1st Cir. 1963)	27
Grin v. *Shine*, 187 U.S. 181 (1902)	17
Gustafson v. *Alloyd Co.*, 513 U.S. 561 (1995)	24
Hamling v. *United States*, 418 U.S. 87 (1974)	32
Liparota v. *United States*, 471 U.S. 419 (1985)	12, 20
McMillan v. *Pennsylvania*, 477 U.S. 79 (1986)	10, 12
Morissette v. *United States*, 342 U.S. 263 (1952)	8, 14, 15, 18, 32, 33
National Organization for Women, Inc. v. *Scheidler*, 510 U.S. 249 (1994)	13
OWCP v. *Greenwich Collieries*, 512 U.S. 267 (1994)	27
Piper v. *Chris-Craft Indus.*, 430 U.S. 1 (1977)	24

Cases—Continued: Page

Ramirez v. *United States*, 318 F.2d 155 (9th Cir. 1963) 27, 28
Ratzlaf v. *United States*, 510 U.S. 135 (1994) 21, 22
Russello v. *United States*, 464 U.S. 16 (1983) 17
Seals v. *United States*, 221 F.2d 243 (8th Cir. 1955) 27
Spies v. *United States*, 317 U.S. 492 (1943) 21
Staples v. *United States*, 511 U.S. 600 (1994) 12, 20
United States v. *Acree*, 466 F.2d 1114 (10th Cir. 1972), cert. denied, 410 U.S. 913 (1973) 27
United States v. *Arthur*, 544 F.2d 730 (4th Cir. 1976) 27
United States v. *Bates*, 852 F.2d 212 (7th Cir. 1988) 8
United States v. *Beattie*, 594 F.2d 1327 (9th Cir. 1979) 28
United States v. *Bishop*, 412 U.S. 346 (1973) 21
United States v. *Britton*, 207 U.S. 655 (1883) . 20, 21, 26
United States v. *Cades*, 495 F.2d 1166 (3d Cir. 1974) 27
United States v. *Cooper*, 577 F.2d 1079 (6th Cir.), cert. denied, 439 U.S. 868 (1978) 29
United States v. *Culbert*, 435 U.S. 371 (1978) 13
United States v. *Docherty*, 468 F.2d 989 (2d Cir. 1972) 27, 28
United States v. *Jakeway*, 783 F. Supp. 590 (M.D. Fla. 1992) 8
United States v. *Kammer*, 1 F.3d 1161 (11th Cir. 1993) 8, 14, 32-33
United States v. *Lanier*, 117 S. Ct. 1219 (1997) 28
United States v. *Logsdon*, 132 F. Supp. 3 (W.D. Ky. 1955), aff'd, 25 F.2d 12 (6th Cir. 1958) 27, 28, 29
United States v. *Mann*, 517 F.2d 259 (5th Cir. 1975) 29
United States v. *Matot*, 146 F.2d 197 (2d Cir. 1944) 29

Cases—Continued: Page

United States v. *Michael*, 456 F. Supp. 335 (D.N.J. 1978) 28
United States v. *Mullins*, 355 F.2d 883 (7th Cir.), cert. denied, 384 U.S. 942 (1966) 27
United States v. *Murdock*, 290 U.S. 389 (1933) 21
United States v. *Pollack*, 503 F.2d 87 (9th Cir. 1974) 28
United States v. *Pomponio*, 429 U.S. 10 (1976) 8, 21
United States v. *Ross*, 77 F.3d 1525 (7th Cir. 1996) 25-26
United States v. *Shabani*, 513 U.S. 10 (1994) 13
United States v. *Vannatta*, 189 F. Supp. 937 (D. Haw. 1960) 29
United States v. *Wells*, 117 S. Ct. 921 (1997) 12, 13, 28, 30, 31
United States v. *X-Citement Video*, 513 U.S. 64 (1994) 20
United States v. *Yermian*, 468 U.S. 63 (1984) 19

Statutes, regulations and rule:

Act of June 3, 1864, ch. 106, § 55, 13 Stat. 116 26
Act of June 15, 1917, Tit. IX, ch. 30, § 2, 40 Stat. 227 (codified at 18 U.S.C. 1542) 18
Comprehensive Employment and Training Act, 18 U.S.C. 665(a) 15
Education Amendments of 1976, Pub. L. No. 94-482, Tit. I, § 127(a), 90 Stat. 2141 23
Education Amendments of 1980, Pub. L. No. 96-374, § 451(a), 94 Stat. 1453 ..... 17, 24
False Statements Accountability Act of 1996, Pub. L. No. 104-292, § 2, 110 Stat. 3459 19
Higher Education Act of 1965, Pub. L. No. 89-529, Tit. IV, Pt. B, 79 Stat. 1236 (codified at 20 U.S.C. 1070 *et seq.*) 3

Statutes, regulations and rule—Continued: Page

Higher Education Amendments of 1992, Pub. L. No. 102-325, 106 Stat. 448:
- Tit. IV, § 411(a)(1), 106 Stat. 510 3
- Tit. IV, § 495, 106 Stat. 631 24

Hobbs Act of 1948, 18 U.S.C. 1951 13
Money Laundering Suppression Act of 1994, Pub. L. No. 103-325, Tit. IV, § 411, 108 Stat. 2253 22
Rev. Stat. § 5209 (1875) 20, 26
7 U.S.C. 2028(d) 15
12 U.S.C. 592 (1925) 26
12 U.S.C. 630 16
15 U.S.C. 645(b) 16
15 U.S.C. 714m(b) 16
18 U.S.C. 2 7
18 U.S.C. 371 13
18 U.S.C. 641 ..... 14, 18
18 U.S.C. 655 (1976) 24
18 U.S.C. 656 ..... 7, 8, 16, 26, 27, 29, 30, 31
18 U.S.C. 656 (Supp. III 1948) (Reviser's note) 27
18 U.S.C. 657 16
18 U.S.C. 660 16
18 U.S.C. 669(a) 16
18 U.S.C. 1001 19
18 U.S.C. 1014 12
18 U.S.C. 1163 16
18 U.S.C. 1962(c) 13
20 U.S.C. 1069d 15
20 U.S.C. 1078(a) 3
20 U.S.C. 1078(b)(1) 3
20 U.S.C. 1078(b)(1)(A) 3
20 U.S.C. 1078(b)(1)(G) 3
20 U.S.C. 1078(b)(1)(N) 3, 32
20 U.S.C. 1078(c) 3
20 U.S.C. 1087-1 3
20 U.S.C. 1087-4 (1976) 17, 23
20 U.S.C. 1092(a)(1)(F) 4, 25, 32
20 U.S.C. 1094(a) 4
20 U.S.C. 1094(a)(1) 3, 25
20 U.S.C. 1094(a)(3) 3

Statutes, regulations and rule—Continued: Page

20 U.S.C. 1097 (1988) 2, 1a-2a
20 U.S.C. 1097 ..... 7, 17, 23
20 U.S.C. 1097(a) (1988) 1-2, 10
20 U.S.C. 1097(a) ..... *passim*
20 U.S.C. 1097(d) 10-11, 17
21 U.S.C. 846 ..... 12, 13
25 U.S.C. 450d 15
31 U.S.C. 5322(a) (1988) 22
31 U.S.C. 5324(3) (1988) 22
42 U.S.C. 1760(g) 15
42 U.S.C. 1761(*o*)(2) 15
42 U.S.C. 2703 (1970) 24
42 U.S.C. 3220(b) 16
42 U.S.C. 3791 (1976) 24
42 U.S.C. 3795 16
34 C.F.R.:
- Section 668.12(b) 4
- Section 668.23 33
- Section 668.82 3
- Section 668.165(b)(4) (1995) 25
- Section 682.600(b) 4
- Section 682.604(b)(1) 3
- Section 682.604(c) 3, 4, 32
- Section 682.604(c)(2) 4
- Section 682.604(d) 4, 32
- Section 682.604(d)(1)(ii) 4, 25
- Section 682.604(d)(1)(ii)(B) (1993) 25
- Sections 682.605-682.607 ..... 4, 32, 33
- Section 682.607 ..... 4, 25

Sup. Ct. R. 24.1(a) 32

Miscellaneous:

9A J. Appelman & J. Appleman, *Insurance Law and Practice* (1981) 30
E. Devitt, *et al.*, *Federal Jury Practice and Instructions*: 21
- Vol. 1 (4th ed. 1992) 21
- Vol. 2 (4th ed. 1990) 30-31

Miscellaneous—Continued: Page

H.R. Conf. Rep. No. 1701, 94th Cong., 2d Sess. (1976) 23
H.R. Rep. No. 1086, 94th Cong., 2d Sess. (1976) 23-24
H.R. Rep. No. 520, 96th Cong., 1st Sess. (1979) 24
H.R. Rep. No. 630, 102d Cong., 2d Sess. (1992) 26
Model Penal Code (1985) 21
VI *The Oxford English Dictionary* (1978) 14
The Random House Dictionary of the English Language (2d ed. 1966) 14
The Random House Dictionary of the English Language (1987) 14
Webster's International Dictionary of the English Language (2d ed. 1958) 14
Webster's Third New International Dictionary (1986) 14

In the Supreme Court of the United States

OCTOBER TERM, 1996

No. 96-7185

GARRIT BATES, PETITIONER

v.

UNITED STATES OF AMERICA

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A1-A13) is reported at 96 F.3d 964. The opinion of the district court (Pet. App. A14-A23) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on September 20, 1996. The petition for a writ of certiorari was filed on December 18, 1996. The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

STATUTORY PROVISION INVOLVED

At the time of the offenses charged in the indictment, Section 1097(a) of Title 20 (1988) provided, in pertinent part:

> Any person who knowingly and willfully embezzles, misapplies, steals, or obtains by fraud, false

> statement, or forgery any funds, assets, or property provided or insured under this subchapter * * * shall be fined not more than $10,000 or imprisoned for not more than 5 years, or both.[1]

As amended in 1992, Section 1097(a) of Title 20 provides, in pertinent part:

> Any person who knowingly and willfully embezzles, misapplies, steals, obtains by fraud, false statement, or forgery, or fails to refund any funds, assets, or property provided or insured under this subchapter * * * shall be fined not more than $20,000 or imprisoned for not more than 5 years, or both.

STATEMENT

On September 8, 1994, a federal grand jury returned a 12-count indictment in the United States District Court for the Northern District of Indiana charging that, on 12 separate occasions between January 15 and June 15, 1990, petitioner knowingly and willfully misapplied federally guaranteed student loan funds, in violation of 20 U.S.C. 1097(a). Before trial, the district court granted petitioner's motion to dismiss the indictment on the ground that the indictment failed to allege intent to injure or defraud the United States as an essential element of an offense under Section 1097(a). Pet. App. A14-A23. The court of appeals reversed, holding that a conviction for knowing and willful misapplication of funds under Section 1097(a) does not require proof of a defendant's intent to injure or defraud the United States. *Id.* at A1-A13.

---

[1] The full text of 20 U.S.C. 1097 (1988) is set forth in the Appendix to the brief.

1. Title IV, Part B of the Higher Education Act of 1965 (HEA), as amended, 20 U.S.C. 1070 *et seq.*, establishes a set of programs commonly known as the Guaranteed Student Loan (GSL) program.[2] The GSL program encourages lenders to make funds available to students who might not otherwise be able to obtain or afford commercial loans to finance the costs of post-secondary education. Under the GSL program, banks that loan money to students receive a guarantee from state or other non-profit organizations that loans will be repaid if borrowers default. 20 U.S.C. 1078(b)(1)(A) and (G). That guarantee is reinsured by the Department of Education. 20 U.S.C. 1078(b)(1) and (c). Additionally, the Department of Education provides interest-rate subsidies and special allowances to lenders on behalf of student borrowers. 20 U.S.C. 1078(a), 1087-1.

Under the GSL program, a school receives loan proceeds directly from the lender. 20 U.S.C. 1078(b)(1)(N); 34 C.F.R. 682.604(b)(1) and (c).[3] If the school does not deliver the loan proceeds to the student, the school must apply the loan proceeds to

---

[2] In 1992, Congress renamed the GSL program the Federal Family Education Loan Program. Higher Education Amendments of 1992, Pub. L. No. 102-325, § 411(a)(1), 106 Stat. 510. Because the conduct at issue in this case is alleged to have occurred before 1992, we refer to the program as the GSL program. Similarly, we refer to the HEA and regulations in effect in 1990, unless otherwise indicated.

[3] Schools must apply the funds "solely for the purposes specified in * * * the provision of [the HEA] program," 20 U.S.C. 1094(a)(1), and must maintain adequate administrative and fiscal procedures to ensure proper administration of, and accounting for, HEA funds, 20 U.S.C. 1094(a)(3); 34 C.F.R. 668.82.

current tuition charges. 34 C.F.R. 682.604(c) and (d).[4] If a student withdraws from the school before completion of a term, the school is required to refund "unearned" amounts of the loan to the lender. 20 U.S.C. 1092(a)(1)(F); 34 C.F.R. 682.605-682.607.[5] Knowing and willful action that impairs the integrity of guaranteed student loan funds, including "misappl[ication]" of those funds, is a criminal offense. 20 U.S.C. 1097(a).

2. Each count of the indictment (J.A. 2-12) incorporates the following factual allegations: James and Laurenda Jackson were the owners and operators of Education America, Inc., a for-profit consulting and management firm for technical and vocational schools. In December 1986, the Jacksons purchased the Acme Institute of Technology, a not-for-profit technical school located in South Bend, Indiana. Petitioner, who was Vice-President of Education America, became Treasurer of the Board of Trustees of Acme. J.A. 2. On April 30, 1987, Mr. Jackson, on behalf of Acme, signed a program participation agreement with the Department of Education, which required compliance with the HEA and regulations governing the GSL program.[6] Petitioner had signed a similar participation agreement on behalf of a different school owned by Education America. J.A. 3.

---

[4] The school must deliver funds that exceed current tuition payments to the student or, with the student's written permission, credit the student's account at the school by that amount for the student's use for the remainder of the academic year. 34 C.F.R. 682.604(c)(2) and (d)(1)(ii).

[5] Schools must establish and publish a refund policy, 20 U.S.C. 1092(a)(1)(F); 34 C.F.R. 682.606(a), and must make refunds to lenders within 60 days following a student's withdrawal, 34 C.F.R. 682.607.

[6] See 20 U.S.C. 1094(a); 34 C.F.R. 668.12(b), 682.600(b).

Acme's tuition refund policy, which was set forth in Acme's catalog and student enrollment agreement and application for admission, provided that tuition would be refunded to students according to the length of the school term remaining at the time of the student's withdrawal. *Ibid.* Acme used a special bank account that segregated unearned tuition income from the school's general account. Acme's former owners utilized the special account to ensure the availability of monies to make refunds to lenders. J.A. 4.

Beginning in late 1987, petitioner and the Jacksons began a pattern and practice of failing to refund GSL program funds. J.A. 4. On April 14, 1988, Mr. Jackson instructed the director of Acme to remit 10% of Acme's monthly gross receipts to Education America as a management fee, and to arrange for a specified monthly salary to be paid by Acme to the Jacksons. In the event that those payments created a shortfall, Education America agreed to loan the money back to Acme. By September 1988, Acme owed lenders approximately $55,000 in overdue refunds. *Ibid.*

In late 1988 or very early 1989, Education America officials instructed Acme to discontinue using the special bank account from which Acme disbursed student loan refunds. In January 1989, when Acme's refund liability reached $68,000, Acme's Financial Aid Director sent a letter to Mr. Jackson indicating the serious nature of the unpaid refunds. J.A. 4. During that time, petitioner began determining on a weekly or daily basis which bills Acme would pay. Petitioner also determined that payments to the Jacksons and Education America would be given priority over making refund payments to lenders following student withdrawals. In so doing, petitioner specifically di-

rected Acme employees not to make refund payments. By March 1989, Acme's refund liability grew to $85,000. J.A. 5.

On March 13, 1989, petitioner, as Executive Vice-President of Education America, wrote to Acme's Financial Aid Director. The letter notified the Financial Aid Director that, at her request, she was released from all responsibility for making loan refunds, and that refunds of unearned tuition would be "solely the responsibility and decision of the corporate office." J.A. 5. The letter also instructed the Financial Aid Director to continue preparing refund documents to be approved by the corporate office for payment. *Ibid.*

In May 1989, a national accrediting association, the National Association of Trade and Technical Schools (NATTS), issued a report following an on-site audit of Acme. NATTS's report concluded that Acme had "inadequately demonstrated its ability to make appropriate and timely refunds, [and had also] loaned substantial amounts of money to the chief trustee and a non-related profit making institution." J.A. 5. The report also noted evidence of "upstreaming" of management fees to Education America and Mr. Jackson. *Ibid.* Acme subsequently lost its accreditation. On April 7, 1990, the Department of Education notified Acme that, effective March 8, 1990, it was no longer eligible to participate in the GSL program. On June 5, 1990, when Acme ceased operations, Acme's accrued total refund debt was $139,649, excluding interest and special allowances. J.A. 5-6.

3. On September 8, 1994, a federal grand jury returned a 12-count indictment against petitioner. The indictment charged that on 12 separate occasions between January 15 and June 15, 1990, petitioner knowingly and willfully misapplied federally guaranteed student loan funds, in violation of 20 U.S.C. 1097(a) and 18 U.S.C. 2. Pet. App. A4.

On February 7, 1995, petitioner filed a motion to dismiss the indictment. Petitioner argued that the offense of misapplication under Section 1097 required proof of (1) a conversion of guaranteed student loan funds, and (2) fraudulent intent. Petitioner further contended that the indictment was defective for failing to allege facts constituting conversion and fraudulent intent. The district court held that the essential elements of a misapplication offense under Section 1097(a) include "(1) that the funds described in the indictment were provided and insured under [Title IV of the HEA] at the time alleged; (2) that the defendant willfully and knowingly misapplied such funds [by converting them to the defendant's own use or the use of another]; and (3) that he did so with an intent to injure or defraud the United States." Pet. App. A22. Because the indictment did not allege that petitioner committed the alleged acts "with an intent to injure or defraud the United States," the court dismissed the indictment as being "insufficient on its face." *Id.* at A23.

4. The court of appeals reversed. Pet. App. A1-A13. The court observed that the Eleventh Circuit and a district court from within that Circuit have read into the offense of misapplication under Section 1097 an additional element of intent to defraud on the ground that courts have read "an intent to injure or defraud" element into the crime of misapplication of bank funds under 18 U.S.C. 656.[7] Pet. App. A7 (citing

---

[7] Section 656 provides that "[w]hoever, being an officer, director, agent or employee of, or connected in any capacity

United States v. *Kammer*, 1 F.3d 1161, 1165 (1993), and *United States* v. *Jakeway*, 783 F. Supp. 590, 597 (M.D. Fla. 1992)). The court of appeals explained, however, that an "[i]ntent to injure or defraud the bank is not subsumed within the phrase 'willful misapplication,' but rather is a separate and distinct component of [Section] 656" that "must be proved *in addition to* willful misapplication." *Id.* at A8. The court also stated that "the language of [Section] 656, like that of [Section] 1097(a), does not explicitly require the defendant to have acted with specific fraudulent or injurious intent." *Ibid.* The court found "a historical rationale" for reading that mental element into Section 656, however, because language requiring an intent to injure or defraud the bank had been "inadvertently dropped in the course of a technical revision of the criminal code." *Id.* at A8-A9 (quoting *United States* v. *Bates*, 852 F.2d 212, 215 (7th Cir. 1988)). In contrast, "Section 1097(a) has never included a requirement that the defendant have acted with an intent to injure or defraud the government." *Id.* at A9. Because there is "no textual or historical basis for doing so," the court declined "to read such a requirement into the statute." *Ibid.* "Rather," the court concluded, "the government must prove that the defendant misapplied—i.e., converted—Title IV funds and that he did so knowingly and willfully." *Id.* at A10.

The court explained that "[c]onversion may include misuse or abuse of property [and] it may reach use in

---

with any * * * [listed bank], embezzles, abstracts, purloins or willfully misapplies any of the moneys, funds or credits of such bank * * * shall be fined not more than $1,000,000 or imprisoned not more than 30 years, or both."

an unauthorized manner or to an unauthorized extent of property placed in one's custody for limited use." Pet. App. A11 (quoting *Morissette* v. *United States*, 342 U.S. 240, 272 (1952)). The court also noted that this Court in *United States* v. *Pomponio*, 429 U.S. 10, 12-13 (1976) (per curiam), which involved a criminal tax prosecution, had defined "willfulness as the 'voluntary, intentional violation of a known legal duty.'" Pet. App. A10. The court concluded that, "as a working definition, willful misapplication under [Section] 1097(a) requires the government to allege and prove that the defendant consciously, voluntarily, and intentionally exercised unauthorized control or dominion over federally provided or guaranteed Title IV funds that interfered with the rights of the funds' true owner(s), for the use and benefit of the defendant or a third person, while knowing that such an exercise of control or dominion over the funds was a violation of the law." *Id.* at A11.

The court of appeals also held, contrary to petitioner's contention, that the indictment alleged sufficient facts to constitute conversion, because the indictment sufficiently charged that petitioner's "handling of federally guaranteed funds was * * * 'unauthorized.'" Pet. App. A12.[8] Because it con-

---

[8] The court of appeals observed that the indictment alleged "(1) that [Acme] had a duty to refund unearned student loans to the lender within thirty to sixty days; (2) that due to the participation agreement and the warnings of Acme's financial aid director, [petitioner] knew of this duty; (3) that [petitioner] specifically directed Acme personnel not to make refunds that were required by law; and (4) that [petitioner] instead made management and salary payments to the Jacksons and to Education America, of which [petitioner] happened to be vice president." Pet. App. A12. Those allegations, the court

cluded that the indictment "included all of the requisite elements of willful misapplication" under Section 1097(a), the court of appeals vacated the district court's judgment dismissing the indictment. *Id.* at A13.

SUMMARY OF ARGUMENT

A. The definition of the elements of a criminal offense is entrusted to the legislature, and "in determining what facts must be proved beyond a reasonable doubt the * * * legislature's definition of the elements of the offense is usually dispositive." *McMillan* v. *Pennsylvania*, 477 U.S. 79, 85 (1986). Section 1097(a) provided, at the time of the offenses charged in this case, that "[a]ny person who knowingly and willfully embezzles, misapplies, steals, or obtains by fraud, false statement, or forgery" student loan funds in amounts exceeding $200 is guilty of a felony. 20 U.S.C. 1097(a) (1988). The text of Section 1097(a) does not contain a requirement that a defendant misapply funds "with an intent to injure or defraud the United States." Rather, the statute contains an express *mens rea* requirement—that the defendant act "knowingly and willfully."

The structure of the statute is also inconsistent with implying an "intent to injure or defraud" element into a misapplication offense. The statute makes it a crime to misapply student loan funds *or* to obtain those funds by fraud, thus indicating that misapplication is a separate offense from the fraudulent acquisition of funds. In addition, Section 1097(d) makes it a felony when a person "knowingly and

---

held, "clearly make out a charge that [petitioner's] handling of Acme's federally guaranteed student loan funds was unauthorized." *Ibid.*

willfully destroys or conceals any record relating to the provision of [Title IV] assistance * * * with intent to defraud the United States." Congress's inclusion of specific language requiring an intent to defraud in subsection (d) but not in subsection (a) confirms that Congress did not intend a misapplication offense under Section 1097(a) to require an intent to defraud.

An "intent to injure or defraud" element cannot be gleaned from the statute's mental element that the defendant act "knowingly and willfully." Those terms require proof that a defendant be aware of the facts constituting the violation and the defendant act intentionally, such that the misapplication of funds prohibited by Section 1097(a) amounts to a criminal conversion. The phrase "knowingly and willfully" does not require proof of an intent to injure or defraud, or proof that the defendant was aware of the illegality of his conduct.

Section 1097(a)'s history provides no support for construing the misapplication offense to require proof of an intent to injure or defraud. Nor does the 1992 amendment to Section 1097(a), which makes it a separate offense to fail to refund student loan proceeds, indicate that an intent to injure or defraud is an element of the offense.

Finally, Section 1097(a) should not be read to incorporate prior judicial constructions of 18 U.S.C. 656, which proscribes willful misapplication of bank funds. Lower courts have read into Section 656 "an intent to injure or defraud" element based on the fact that direct antecedents of that statute had contained such a requirement until the statute was recodified in 1948. Section 1097(a) has no similar history, however, and there was no settled understanding at the time

Congress enacted Section 1097(a) that the words "willfully misapplies" inherently require an element of an intent to defraud or injure.

B. The indictment in this case, which alleges that petitioner knowingly and willfully misapplied student loan funds by failing to refund those funds when due, sufficiently alleges that petitioner committed misapplication in violation of Section 1097(a). Because an intent to injure or defraud is not an element of the offense, an allegation of such intent is unnecessary.

ARGUMENT

A. "Intent To Injure Or Defraud" Is Not An Element Of The Offense Defined By 20 U.S.C. 1097(a)

1. This Court often has emphasized that "[t]he definition of the elements of a criminal offense is entrusted to the legislature, particularly in the case of federal crimes, which are solely creatures of statute." *Staples* v. *United States*, 511 U.S. 600, 604 (1994) (quoting *Liparota* v. *United States*, 471 U.S. 419, 424 (1985)). Thus, "in determining what facts must be proved beyond a reasonable doubt the * * * legislature's definition of the elements of the offense is usually dispositive." *McMillan* v. *Pennsylvania*, 477 U.S. 79, 85 (1986).

The primary source for identifying the elements of a criminal offense is the statutory text, and this Court has often declined to add elements that have no basis in that text. Most recently, in *United States* v. *Wells*, 117 S. Ct. 921 (1997), this Court held that materiality is not an element of the crime of knowingly making a false statement to a federally insured bank under 18 U.S.C. 1014. Examining the text of Section 1014, which did not "so much as mention materiality," the Court concluded that, "under the first

criterion in the statutory interpretation hierarchy," materiality is not an element of the offense. 117 S. Ct. at 927. Similarly, in *United States* v. *Shabani*, 513 U.S. 10 (1994), the Court unanimously rejected the argument that courts should read into the drug conspiracy statute, 21 U.S.C. 846, a requirement that a conspirator have committed an overt act in furtherance of the conspiracy. The Court noted that, unlike the general conspiracy statute, 18 U.S.C. 371, the text of Section 846 does not contain an overt act requirement. The Court accordingly held that, "[i]n light of this additional element in the general conspiracy statute, Congress' silence in [Section] 846 speaks volumes." 513 U.S. at 14; see also *National Organization for Women, Inc.* v. *Scheidler*, 510 U.S. 249, 256-257 (1994) (rejecting argument that 18 U.S.C. 1962(c) requires proof of economic motive, and noting that "[n]owhere in [the statute] is there any indication that, an economic motive is required"); *United States* v. *Culbert*, 435 U.S. 371, 373, 380 (1978) (rejecting claim that, to establish violation of the Hobbs Act, 18 U.S.C. 1951, it must be shown that defendant engaged in "racketeering" activities, and noting that "the absence [in the statute] of any reference to 'racketeering' * * * is strong evidence that Congress did not intend to make 'racketeering' an element of a Hobbs Act violation").

The principle that Congress's definition of the elements of a criminal offense is generally controlling compels the conclusion that the knowing and willful misapplication of federally insured student loan funds in violation of 20 U.S.C. 1097(a) does not require proof that the defendant acted with an intent to injure or defraud. No such words appear in the

definition of the misapplication offense. Nor are such concepts implicit in the word "misapply".[9]

Petitioner concedes (Br. 3, 7), and the courts of appeals agree (Pet. App. A10-A11; *United States* v. *Kammer*, 1 F.3d 1161, 1165 (11th Cir. 1993)), that misapplication under Section 1097(a) is a species of conversion. In construing 18 U.S.C. 641, which punishes one who "embezzles, steals, purloins, or knowingly converts to his own use or the use of another" government property, this Court in *Morissette* v. *United States*, 342 U.S. 246 (1952), observed that conversion may occur "without any intent to keep and without any wrongful taking" and "may reach use [of property] in an unauthorized manner or to an unauthorized extent." *Id.* at 271-272. Although the Court in *Morissette* held that "mere omission from [Section] 641 of any mention of intent will not be construed as eliminating that element from the crimes denounced," *id.* at 263, the Court also concluded that the *mens rea* requirement of the statute is satisfied if the defendant "had knowledge of the

[9] At the time of enactment of the misapplication offense, as now, the standard dictionary definition of the word "misapply" confirms that the word "misapply" does not connote "fraud." See, *e.g.*, *The Random House Dictionary of the English Language* 1228 (2d ed. 1987) ("misapply" means "to make a wrong application or use of"); *Webster's Third New International Dictionary* 1442 (1986); ("misapply" means "to apply wrongly"); VI *The Oxford English Dictionary* 494 (1978) ("misapply" means "[t]o apply to a wrong person or object; to make a wrong application of"); *The Random House Dictionary of the English Language* 914 (1966) ("misapply" means "to make a wrong application or use of"); *Webster's New International Dictionary of the English Language* 1568 (2d ed. 1958) ("misapply" means "[t]o apply wrongly; to use for a wrong purpose").

facts, though not necessarily the law, that made the taking a conversion," *id.* at 271. Similarly, misapplication under Section 1097(a), like the crime of conversion, requires proof of misuse or unauthorized use of federally insured student loan proceeds for the benefit of the defendant or a third party. Unlike the statute in *Morissette*, Section 1097(a) has an express *mens rea* element—that the defendant misapply funds "knowingly and willfully"—and that element requires only that the defendant be aware that his use of the funds is unauthorized or wrongful and that he act intentionally. There is no basis for reading into the statute an additional *mens rea* requirement of an intent to injure or defraud.

Indeed, Congress separately addressed the fraudulent acquisition of student loan funds in Section 1097(a). That provision makes it an offense to "obtain[]" student loan funds "by fraud."[10] The fact

[10] Section 1097(a) is worded similarly to a number of statutes employing the words "willfully" and "misapplies" that punish persons who take or misuse federally provided or insured funds. Some of those statutes, like Section 1097(a), also separately prohibit fraud. See, *e.g.*, 7 U.S.C. 2028(d) ("[w]hoever knowingly and willfully embezzles, misapplies, steals, or obtains by fraud, false statement, or forgery" food assistance to Puerto Rico); 18 U.S.C. 665(a) ("[w]hoever * * * embezzles, willfully misapplies, steals, or obtains by fraud" funds appropriated under the Comprehensive Employment and Training Act); 20 U.S.C. 1069d ("[w]hoever * * * willfully misapplies, steals, or obtains by fraud" federal educational grants or assistance); 25 U.S.C. 450d ("[w]hoever * * * embezzles, willfully misapplies, steals, or obtains by fraud" Indian self-determination and educational assistance); 42 U.S.C. 1760(g) ("[w]hoever embezzles, willfully misapplies, steals, or obtains by fraud" school lunch program funds); 42 U.S.C. 1761(*o*)(2) ("[w]hoever * * * knowingly or willfully embezzles, misapplies, steals, or

that Congress separately prohibited the fraudulent appropriation of student loan funds strongly suggests that misapplication under Section 1097(a) prohibits a different form of misconduct.

---

obtains by fraud, false statement, or forgery" food service program funds for children in service instiutions); 42 U.S.C. 3795 ("[w]hoever embezzles, willfully misapplies, steals, or obtains by fraud" Department of Justice funds); see also 12 U.S.C. 630 ("[e]very officer * * * who embezzles, abstracts, or willfully misapplies any of the money [of corporations organized to do foreign banking] * * * ; or who makes any false entry * * * with intent * * * to injure or defraud"); 15 U.S.C. 645(b) ("[w]hoever * * * (1) embezzles, abstracts, purloins, or wilfully misapplies any money * * * , or (2) with intent to defraud the [Small Business] Administration * * * makes any false entry * * *, or (3) with intent to defraud participates"); 15 U.S.C. 714m(b) ("[w]hoever * * * (i) embezzles, abstracts, purloins, or wilfully misapplies any money * * *; or (ii) with intent to defraud the [Commodity Credit] Corporation * * * makes any false entry"); 42 U.S.C. 3220(b) ("[w]hoever * * * (1) embezzles, abstracts, purloins, or willfully misapplies [economic development funds] * * *, or (2) with intent to defraud the Secretary [of Health and Human Services] * * * makes any false entry").

There are some other statutes prohibiting misapplication that do not make the crime of fraud a separate offense. See, *e.g.*, 18 U.S.C. 656 ("[w]hoever * * * embezzles, abstracts, purloins or willfully misapplies" bank funds); 18 U.S.C. 657 ("[w]hoever * * * embezzles, abstracts, purloins or willfully misapplies" funds belonging to certain banking institutions); 18 U.S.C. 660 ("[w]hoever * * * embezzles, steals, abstracts, or willfully misapplies" property of a common carrier); 18 U.S.C. 669(a) ("[w]hoever knowingly and willfully embezzles, steals, or * * * converts to the use of any person other than the rightful owner, or intentionally misapplies" any property of a health care benefit program); 18 U.S.C. 1163 ("[w]hoever embezzles, steals, knowingly converts to his use or the use of another, willfully misapplies, or willfully permits to be misapplied" property belonging to Indian tribal organizations).

The overall structure of Section 1097 further shows that Congress did not require proof of an intent to injure or defraud in the misapplication offense. Congress enacted Section 1097(d) at the same time as it enacted Section 1097(a). Education Amendments of 1980, Pub. L. No. 96-374, § 451(a), 94 Stat. 1453; see also 20 U.S.C. 1087-4 (1976) (former criminal penalties under GSL program). Section 1097(d) prohibits the "[o]bstruction of justice" by "[a]ny person who knowingly and willfully destroys or conceals any record relating to the provision of [Title IV] assistance * * * *with intent to defraud the United States*." 20 U.S.C. 1097(d) (emphasis added). The absence of any similar "intent to defraud" language in subsection (a) indicates that Congress did not mean to require any additional element of intent when it prohibited a person from "knowingly and willfully * * * misappl[ying]" student loan funds. See *Russello* v. *United States*, 464 U.S. 16, 23 (1983) ("Where Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion.").

Petitioner argues (Br. 10-11) that Congress included the word "misapplies" in a list of offenses that require proof of scienter, and that the misapplication offense should therefore be construed similarly. The fact that each offense in Section 1097(a) requires an element of criminal intent, however, does not establish that each offense contains the identical requirement. For instance, this Court has stated that "the word 'embezzle' implies a fraudulent intent." *Grin* v. *Shine*, 187 U.S. 181, 190 (1902). This Court has also described the elements of "stealing,"

however, without including fraudulent intent, *Morissette*, 342 U.S. at 271, and has said that there are "intentional and knowing abuses and unauthorized uses of government property that might be knowing conversions but which could not be reached as embezzlement, stealing or purloining," *id.* at 272; see also *id.* at 271 ("Probably every stealing is a conversion, but certainly not every knowing conversion is a stealing."). Thus, the Court in *Morissette* explained that, because "[t]he books contain a surfeit of cases drawing fine distinctions between slightly different circumstances under which one may obtain wrongful advantages from another's property," Congress drafted Section 641 "to reach all such instances." *Id.* at 271. Similarly, the inclusion of multiple forms of misconduct in the text of Section 1097(a) indicates that Congress intended to prohibit a variety of criminal acts directed at student loans funds, not all of which involve fraud.

2. a. Petitioner argues (Br. 11) that, because Section 1097(a) uses the words "knowingly and willfully," Congress intended to require proof of "the highest degree of mental culpability." The phrase "knowingly and willfully," however, does not connote an intent to injure or defraud. In *Browder* v. *United States*, 312 U.S. 335 (1941), the Court considered the meaning of the words "willfully and knowingly" in an Act of Congress that punishes persons who "willfully and knowingly" use a passport obtained by a false statement. See Act of June 15, 1917, ch. 30, Tit. IX, § 2, 40 Stat. 227 (codified at 18 U.S.C. 1542). The Court rejected petitioner's argument that the phrase "willfully and knowingly" signifies a use "which is in itself evil as the use of a passport to invoke fraudulently the protection of the United States abroad." 312 U.S. at 340 (internal quotation marks omitted). The Court explained that "[n]one of [the statute's] words suggest that fraudulent use is an element of the crime." *Id.* at 341. Thus, the Court concluded that "[r]ead in its context the phrase 'willfully and knowingly[]' * * * can be taken only as meaning 'deliberately and with knowledge and not something which is merely careless or negligent or inadvertent.'" *Ibid.*

Similarly, this Court in *United States* v. *Yermian*, 468 U.S. 63 (1984), held that 18 U.S.C. 1001, which makes it an offense when a person "in any matter within the jurisdiction of any department or agency of the United States knowingly and willfully * * * makes any false, fictitious or fraudulent statements," does not require proof of actual knowledge of federal agency jurisdiction. 468 U.S. at 68-69.[11] The Court described the mental element of the statute to require proof of "intentional and deliberate lies," *id.* at 74, but declined to read into the words "knowingly and willfully" "any additional element of intent, such as a requirement that false statements be 'knowingly made in a matter within federal agency jurisdiction,' or 'with the intent to deceive the Federal Government,'" *id.* at 69.

Like the statutes at issue in *Browder* and *Yermian*, there is nothing in the text or structure of Section 1097(a) that signifies that Congress intended that an offense of misapplication include an additional element of an intent to injure or defraud. The more

---

[11] Section 1001 was amended in 1996 without relevant change. False Statements Accountability Act of 1996, Pub. L. No. 104-292, § 2, 110 Stat. 3459.

natural reading of the statute, particularly in light of the statute's separate prohibition of fraudulent conduct and the explicit inclusion of the phrase "intent to defraud" in subsection (d) of the statute, is that an intent to injure or defraud is not an element of the misapplication offense.

Petitioner and his amicus (Pet. Br. 11-13; Amicus Br. 10-12) argue that reading an intent to injure or defraud element into the statute is necessary to prevent the statute from reaching innocent conduct. See *Liparota*, 471 U.S. at 426; *Staples*, 511 U.S. at 610; *United States* v. *X-Citement Video, Inc.*, 513 U.S. 64, 70-72 (1994). A defendant who knowingly and intentionally misuses or converts federally guaranteed student loan funds, however, has not engaged in "apparently innocent conduct." *Liparota*, 471 U.S. at 426.[12]

---

[12] In support of his position, petitioner mistakenly relies (Br. 12) on *United States* v. *Britton*, 107 U.S. 655 (1883). In *Britton*, this Court held that the offense of willful misapplication of bank funds under Revised Statutes Section 5209 (1875) was not charged by an indictment alleging that a bank president had purchased the bank's stock, in contravention of law, and had held the stock in trust for the bank's use. 107 U.S. at 667. The court stated that the offense of "willful misapplication * * * means something different from the acts of official maladministration * * * and it must be a willful misapplication for the use or benefit of the party charged, or of some person or company other than the association, with intent to injure and defraud the association." *Id.* at 668. The statute at issue, however, contained language explicitly requiring that the government prove an intent to injure or defraud the bank or to deceive a bank officer. *Id.* at 655-656; see pp. 26-27, *infra*. Moreover, the Court's conclusion that the indictment had "charge[d] maladministration * * * rather than criminal misapplication" was based on the fact that the defendant's purchase of stock, which the defendant held "in trust" for the bank, was not a "conversion" of the bank's funds. 107 U.S. at 667. In the present case, petitioner has been charged not with poor administration, but with intentionally failing to make refund payments that he knew were due and owing.

b. Relying on the definition of "willfulness" set forth in *United States* v. *Pomponio*, 429 U.S. 10, 12 (1976) (per curiam), the court of appeals held that Section 1097(a) requires that the defendant must "know[] that [the unauthorized] exercise or control or dominion over the funds was a violation of the law." Pet. App. A10, A11. We disagree. The court's conclusion departs from "the venerable principle that ignorance of the law generally is no defense to a criminal charge." *Ratzlaf* v. *United States*, 510 U.S. 135, 149 (1994); see also *Cheek* v. *United States*, 498 U.S. 192, 199 (1991).

This Court has explained that the word "willfully" is a "word of many meanings," and "its construction [is] often . . . influenced by its context." *Ratzlaf*, 510 U.S. at 141 (quoting *Spies* v. *United States*, 317 U.S. 492, 497 (1943)). Standard definitions of "willfully" do not include any requirement of knowledge of illegality. See Model Penal Code §§ 2.02(8) and (9) & cmts. 10, 11 (1985); 1 E. Devitt, *et al.*, *Federal Jury Practice and Instructions* § 17.05 (4th ed. 1992). In the context of federal criminal tax offenses, however, the Court in *Pomponio* reaffirmed that the word "willfully" requires proof of a "voluntary, intentional violation of a known legal duty." 429 U.S. at 12; see *Cheek*, 498 U.S. at 200-204; *United States* v. *Bishop*, 412 U.S. 346, 360 (1973); *United States* v. *Murdock*, 290 U.S. 389, 394-395 (1933). "This special treatment of criminal tax offenses is largely due to the complexity of the tax laws." *Cheek*, 498 U.S. at 200.

Similarly, the Court in *Ratzlaf*, *supra*, held that a prosecution under 31 U.S.C. 5322(a) (1988), which imposes penalties for "[a] person willfully violating," *inter alia*, the antistructuring provision of 31 U.S.C. 5324(3) (1988), requires that a defendant know that currency structuring is illegal.[13] 510 U.S. at 149. The Court reasoned that a failure to construe the word "willfully" as requiring a knowing violation of the law would render the word superfluous in light of Section 5324(3)'s requirement that a currency transaction be structured "for the purpose of evading" reporting requirements. *Id.* at 140-141. Moreover, because the statute's "omnibus 'willfulness' requirement, when applied to other provisions in the same subchapter," consistently has been read to require "a 'specific intent to commit the crime,'" *id.* at 141, the Court found a "strong[] cause to construe a single formulation * * * the same way each time it is called into play" *id.* at 143 (emphasis omitted). Finally, the Court expressed the view that currency structuring in order to avoid reporting requirements "is not inevitably nefarious." *Id.* at 144.

Section 1097(a), however, lacks the distinctive contextual features found in the tax and antistructuring statutes that justified a departure from the general rule that ignorance of the law is no defense. See *Cheek*, 498 U.S. at 199. Unlike the tax statutes, there is no danger that a defendant who engages in the knowing and intentional conversion covered by

[13] Following the Court's decision in *Ratzlaf*, Congress amended the relevant provisions to provide that an antistructuring offense does not require proof of knowledge of illegality. See Money Laundering Suppression Act of 1994, Pub. L. No. 103-325, Tit. IV, § 411, 108 Stat. 2253.

Section 1097(a) might inadvertently commit an offense. And unlike the crime of structuring currency transactions, there is no underlying regulatory prohibition that contains its own *mens rea* requirement. Rather, like the statutes at issue in *Browder* and *Yermian*, the *mens rea* requirement of misapplication under Section 1097(a) is satisfied by knowing and intentional conduct—here, involving consciousness that the use of property is unauthorized. See pp. 14-15, *supra*.

3. The history of Section 1097 does not indicate that Congress intended the misapplication offense to require proof of an intent to injure or defraud. Congress first added criminal penalties to Section 440 of the Higher Education Act of 1965 in the Education Amendments of 1976, Pub. L. No. 94-482, § 127(a), 90 Stat. 2141. Those penalties were codified at 20 U.S.C. 1087-4 (1976) and applied only to GSL program funds. See H.R. Conf. Rep. No. 1701, 94th Cong., 2d Sess. 196-197 (1976). A House Report to the 1976 Amendments indicates that criminal penalties were enacted "[a]s a deterrent to those unscrupulous individuals who would willfully and knowingly embezzle, misapply, steal or obtain by fraud, false statement or forgery, student aid funds." H.R. Rep. No. 1086, 94th Cong., 2d Sess. 12 (1976). There is no indication that Congress intended to punish only those individuals who abused the GSL program with an intent to injure or defraud.[14]

[14] The House Report also included a letter written by Assistant Attorney General Michael Uhlmann that endorsed an earlier version of the bill containing similar language to Section 440(a). The letter stated that the bill's "language tracks fraud sections elsewhere in the United States Code (see 42 U.S.C. 2703, 42 U.S.C. 3791 and 18 U.S.C. 655)." H.R. Rep. No. 1086,

Congress enacted Section 1097 as part of the Education Amendments of 1980 to extend the HEA's criminal penalties to all programs funded under Title IV. Pub. L. No. 96-374, § 451(a), 94 Stat. 1453; H.R. Rep. No. 520, 96th Cong., 1st Sess. 46 (1979). The statute's sparse legislative history contains no suggestion that Congress wanted to limit the criminal penalties in the Act only to conduct constituting fraud.

Petitioner argues (Br. 13-15) that one can infer that Congress knew that misapplication under Section 1097(a) required proof of intent to defraud, because the statute was amended in 1992 to punish an individual who "fails to refund" federally insured student loan funds (see Higher Education Amendments of 1992, Pub. L. No. 102-325, Tit. IV, § 495, 106 Stat. 631). Petitioner argues (Br. 15) that, "[h]ad fraudulent intent not been an element of 'misapplication,'" the government could have brought conduct within the reach of the statute by promulgating regulations "severely restricting the use of funds."

Petitioner's argument is based on the mistaken assumption that, at the time of the conduct charged in the indictment, the "regulatory scheme * * * did not

---

supra, at 12. Even if that letter were viewed as an indication of legislative intent, the letter does not suggest that the word "misapplies" signifies fraudulent conduct. Cf. *Gustafson* v. *Alloyd Co.*, 513 U.S. 561, 580 (1995); *Piper* v. *Chris-Craft Indus., Inc.*, 430 U.S. 1, 31 n.20 (1977). While the letter compared the bill to "fraud sections," one of the statutory references, 18 U.S.C. 655 (1976), punishes theft by bank examiners and mentions neither the word "fraud" nor "misapply," and the other two references, 42 U.S.C. 2703 (1970) and 42 U.S.C. 3791 (1976), punish any person who either "willfully misapplies" or "obtains by fraud" government property.

stringently restrict the use of student loan proceeds by a school." Br. 15. To support that proposition, however, petitioner relies (Br. 14) solely on the fact that the Department of Education, over time, has changed the accounting requirements for loan proceeds when a lender delivers funds to a school in excess of current tuition charges, and the student requests in writing that the school retain the funds for the student's benefit. 34 C.F.R. 682.604(d)(1)(ii); see note 4, *supra*. Effective July 1, 1993, schools were required to maintain those funds in a designated trust account and were prohibited from commingling them with the school's other funds. 34 C.F.R. 682.604(d)(1)(ii)(B) (1993). Effective July 1, 1995, schools may retain such funds if the school identifies the student and the amount of funds in a "subsidiary ledger account designated for that purpose" and the school maintains "cash in its bank for an amount at least equal to the amount of the funds the institution holds for the student." 34 C.F.R. 668.165(b)(4) (1995).

Those rules, however, in no way alter the requirements in effect in 1990 that schools may apply HEA funds "solely for the purpose specified in and in accordance with the provision of [the HEA] program," 20 U.S.C. 1094(a)(1); that schools establish and publish a "refund policy * * * for the return of unearned tuition and fees or other refundable portion of cost," 20 U.S.C. 1092(a)(1)(F); or that schools refund unearned program funds to lenders following a student's withdrawal, 34 C.F.R. 682.607. Accordingly, even before the 1992 amendment of Section 1097(a), the offense of misapplication encompassed a defendant's deliberate failure to refund loan proceeds that the defendant knew no longer belonged to the school. See *United States* v. *Ross*, 77 F.3d 1525, 1541 (7th Cir.

1996) ("failing to make refunds constituted misapplication within the meaning of [Section] 1097(a) even prior to its amendment").[15] Thus, there is nothing in the 1992 amendment or regulations under the HEA that suggests that Congress intended the offense of misapplication to require proof of an intent to injure or defraud, and certainly no evidence strong enough to overcome the absence of such an element from the statutory text.

4. Amicus Curiae National Association of Criminal Defense Lawyers (NACDL) argues (Br. 6-9) that, by the time Section 1097(a) was enacted in 1980, the offense of "willful misapplication" had a settled meaning that required proof of fraudulent or injurious intent, because courts had required proof of an intent to injure or defraud to establish the criminal misapplication of bank funds under 18 U.S.C. 656 even in the absence of statutory language requiring such proof. That argument lacks merit.

Congress initially created the offense of willful misapplication of bank funds in the Act of June 3, 1864, ch. 106, § 55, 13 Stat. 116. It later appeared as Revised Statutes Section 5209 (1875), see *United States* v. *Britton*, 107 U.S. 655 (1883), and subsequently was codified at 12 U.S.C. 592 (1925). Section 592, like its predecessor versions, included the language "with intent * * * to injure or defraud [the bank] * * *, or

[15] The notion that a defendant's pre-1992 failure to refund student loan proceeds constitutes misapplication is consistent with the 1992 amendment's history. See H.R. Rep. No. 630, 102d Cong., 2d Sess. 513 (1992) ("failure to pay refunds does constitute criminal misapplication under current law. Language is added in this bill merely as clarification."); see also J.A. 40-41 (2/28/92 letter from Sen. Kassebaum to James B. Thomas, Jr., Inspector General, Dep't of Educ.).

to deceive any officer of such [bank]" as an element of the offense. That language was deleted from what is now 18 U.S.C. 656 during the 1948 revision of Title 18 of the Code. The Reviser's note stated that "[t]he revised section without changing in any way the meaning or substance of existing law, clarifies, condenses, and combines related provisions largely rewritten in matters of style." 18 U.S.C. 656 (Supp. III 1948). Based on the peculiar history of Section 656, the lower courts had concluded, before Congress enacted criminal penalties in the HEA, that the offense of willful misapplication of bank funds requires proof of intent to injure or defruad the bank.[16]

Those decisions, however, do not establish that the words "willfully misapplies" have a connotation of requiring intent to injure or defraud that was "generally accepted in the legal community at the time of [the] enactment" of Section 1097(a). *OWCP* v. *Greenwich Collieries*, 512 U.S. 267, 275 (1994). Before Congress made it an offense to misapply student loan funds, courts had not uniformly indicated that the words "willfully misapplies" under Section 656 carry

[16] See, *e.g.*, *Golden* v. *United States*, 318 F.2d 357, 361 (1st Cir. 1963); *United States* v. *Docherty*, 468 F.2d 989, 994-995 (2d Cir. 1972); *United States* v. *Cades*, 495 F.2d 1166, 1168 n.3 (3d Cir. 1974); *United States* v. *Arthur*, 544 F.2d 730, 736 n.11 (4th Cir. 1976); *Garrett* v. *United States*, 396 F.2d 489, 491 (5th Cir.), cert. denied, 393 U.S. 952 (1968); *United States* v. *Logsdon*, 132 F. Supp. 3, 4-5 (W.D. Ky. 1955), aff'd, 253 F.2d 12 (6th Cir. 1958); *United States* v. *Mullins*, 355 F.2d 883, 886 (7th Cir.), cert. denied, 384 U.S. 942 (1966); *Seals* v. *United States*, 221 F.2d 243, 245 (8th Cir. 1955); *Ramirez* v. *United States*, 318 F.2d 155, 157-158 (9th Cir. 1963); *United States* v. *Acree*, 466 F.2d 1114, 1116 (10th Cir. 1972), cert. denied, 410 U.S. 913 (1973).

an implicit element of intent to injure or defraud. Some decisions expressed the view that the omission of the words "intent to injure or defraud" in 1948 was an intentional attempt by the codifier to omit redundant terms. See, *e.g.*, *United States* v. *Logsdon*, 132 F. Supp. 3, 5 (W.D. Ky. 1955), aff'd, 253 F.2d 12 (6th Cir. 1958); *Ramirez* v. *United States*, 318 F.2d 155, 158 (9th Cir. 1963) (agreeing with *Logsdon*). Other decisions, however, expressed the view that the omission was a drafting error necessitating judicial correction. See, *e.g.*, *United States* v. *Pollack*, 503 F.2d 87, 90-91 (9th Cir. 1974) ("those courts which have considered the elimination of the 'intent to injure or defraud' language in [Section] 656, have interpreted such elimination as an oversight" (footnote omitted)); *Docherty*, 468 F.2d at 994 ("courts must be mindful of [Section 656's] history and avoid undue extension as a result of the ill-conceived work of the 1948 reviser").[17] That latter view—one that

[17] Other courts expressed uncertainty as to why the language was deleted. See *United States* v. *Beattie*, 594 F.2d 1327, 1329 (9th Cir. 1979) ("the words 'intent to injure and defraud' in the predecessor statute were omitted (perhaps inadvertently, as the revisers' proposed intention was not to change the meaning of existing law)"); *United States* v. *Michael*, 456 F. Supp. 335, 339 (D.N.J. 1978) (" 'intent to injure or defraud' * * * remains an essential element of the crime * * * notwithstanding the unexplained deletion of those words in the 1948 recodification").

Of course, it is possible that the Reviser may have erred in noting that no substantive change was intended in the 1948 recodification. See *Wells*, 117 S. Ct. at 930 ("Those who write revisers' notes have proven fallible before."); *United States* v. *Lanier*, 117 S. Ct. 1219, 1226 n.6 (1997) ("The legislative intent of Congress is to be derived from the language and structure of the statute itself, if possible, not from the assertions of codifiers

reads the element of an "intent to injure or defraud" back into the statute—necessarily implies that the words "willfully misapply" are insufficient by themselves to require proof of an intent to injure or defraud. Thus, courts have been divided on whether those words inherently incorporated an intent to injure or defraud. Compare *Logsdon*, 253 F.2d at 14 (agreeing with the trial court's conclusion that "the words 'did wilfully misapply' constituted a sufficient charge of a criminal intent to defraud"); *United States* v. *Mann*, 517 F.2d 259, 267 n.3 (5th Cir. 1975) (citing *Ramirez* and noting that "the allegation of willful misapplication sufficiently imports an intent to injure or defraud"); *United States* v. *Matot*, 146 F.2d 197, 198 (2d Cir. 1944) (Hand, J.) (stating that " 'wilful misapplication' [under 12 U.S.C. 592] of money presupposes a fraudulent intent"), with *United States* v. *Cooper*, 577 F.2d 1079, 1082 (6th Cir.) ("in common understanding [the term 'misapplies'] has a somewhat different connotation from that of fraud generally"), cert. denied, 439 U.S. 868 (1978); *United States* v. *Vannatta*, 189 F. Supp. 937, 938-939 (D. Haw. 1960) (disagreeing with *Logsdon* and concluding that allegation of willful misapplication does not encompass an allegation of fraudulent intent).

In sum, judicial decisions pre-dating the enactment of criminal penalties in the HEA had adopted disparate views on whether the words "willfully misapplies" in Section 656 intrinsically incorporated an intent to injure or defraud. Because "[i]t would thus

directly at odds with clear statutory language."). Thus, Congress may have deleted the "intent to injure or defraud" language simply because Congress no longer intended it to be an element of the offense.

be impossible to say which view Congress might have endorsed," *Wells*, 117 S. Ct. at 930, decisions interpreting Section 656 do not support petitioner's construction. See, *e.g.*, *Fogerty* v. *Fantasy, Inc.*, 510 U.S. 517, 527-532 (1994) (rejecting reliance on pre-enactment decisions because although majority of courts had awarded attorneys' fees under predecessor statute, not all courts had expressed a uniform construction of relevant language in statute).[18]

The contention that the offense of willful misapplication under Section 656 had a settled meaning that included an intent to defraud or injure is also undermined by the common understanding of that offense today. As the decision below explained (Pet. App. A8), "willfully misapplies" and "intent to injure or defraud" are treated as separate elements of a Section 656 offense, and each has a distinct meaning. See generally 2 E. Devitt, *et al.*, *Federal Jury Practice and Instructions* § 30.03 (4th ed. 1990) (listing the requirement that defendant "willfully misapplied" bank funds as separate element from requirement

[18] Nor is there any reason to think, as amicus NACDL suggests (Br. 8-9), that Congress had in mind or was even aware of state court decisions construing the words "willful misapplication" in fidelity guarantee contracts. In the context of such contracts, which insure against losses caused by a lack of fidelity or honesty of employees or other persons holding positions of trust, it is hardly surprising that, for the loss to be insured, "it is generally held that the employee's misappropriation or misapplication must be done with a dishonest or fraudulent intent, although it is not necessary that it constitute a crime." See 9A J. Appleman & J. Appleman, *Insurance Law and Practice* § 5670 (1981) (footnote omitted). In contrast, Section 1097(a) applies to anyone who intentionally takes or misuses federal student loan funds, whether or not the defendant holds those funds pursuant to a trust relationship.

that the defendant "did so with the intent to injure or defraud the bank"), § 30.05 (defining "willfully misapplies" as "the unauthorized or unjustifiable or wrongful use of the monies, funds or credits of the bank" and collecting authorities), and § 30.06 (defining "intent to injure or defraud the bank" as "to act knowingly and with the intent to deceive or to cheat the bank" and collecting authorities). In any event, Section 1097(a) and Section 656 are worded differently and there is no indication that Congress patterned the former after the latter. Unlike Section 656, Section 1097(a) makes it a separate offense to "obtain[] [funds] by fraud." The wording of Section 1097(a) thus casts serious doubt on the proposition that Congress intended that the offense of misapplication require proof of intent to injure or defraud.

5. Finally, petitioner contends (Br. 16-17) that, to the extent that Section 1097(a) is ambiguous, the rule of lenity supports an interpretation of the statute to require a showing of an intent to injure or defraud. "Read straightforwardly," however, Section 1097(a) "reveals no ambiguity, its *mens rea* requirements narrow the sweep of the statute, and this is not a case of guesswork reaching out for lenity." *Wells*, 117 S. Ct. at 931. Accordingly, the rule of lenity does not compel reading an intent to injure or defraud into the offense of misapplication under Section 1097(a).

B. The Indictment Sufficiently Alleges The Offense Of Misapplication Under Section 1097(a)

1. Petitioner contends (Br. 19) that the indictment is insufficient for failing to allege that petitioner intended to defraud anyone by the alleged acts. Because intent to defraud is not an element of the misapplication offense under Section 1097(a), how-

ever, an allegation of fraudulent intent is unnecessary. *Hamling* v. *United States*, 418 U.S. 87, 117-118 (1974).

2. Petitioner also argues (Br. 19) that the indictment does not allege facts constituting a conversion of student loan proceeds, because the indictment does not set forth how Acme applied those proceeds. That issue, however, was not raised in the petition for a writ of certiorari and thus is not properly before the Court. See Sup. Ct. R. 24.1(a).

In any event, petitioner's contention is based on a misunderstanding of the HEA and this Court's teaching in *Morissette* that conversion "may be consummated without any intent to keep and without any wrongful taking, where the initial possession by the converter was entirely lawful." 342 U.S. at 271-272. Under the HEA, schools receive loan proceeds directly from lenders. 20 U.S.C. 1078(b)(1)(N); 34 C.F.R. 682.604(c). The school must either disburse the amount of those funds to the student or apply the funds "to credit a registered student's account." 34 C.F.R. 682.604(d). Upon a student's withdrawal from a school, the school is required to refund the "unearned" tuition and other "refundable" charges. 20 U.S.C. 1092(a)(1)(F); 34 C.F.R. 682.605-682.607. Accordingly, even if a school properly credits a student's account by the amount of the student loan proceeds, the funds may be converted, *i.e.*, misapplied, by a failure to make required refunds.[19]

---

[19] In *Kammer*, the Eleventh Circuit held that a school's failure to refund federal educational grant funds is not a conversion under Section 1097(a) because HEA regulations allow a school "to commingle its own monies with federal financial aid funds." 1 F.3d at 1166. The court reasoned that a "financially endangered" school which fails to refund money that it "[does] not have" lacks the "criminal intent to defraud." *Ibid.* The court's decision, however, is based on the incorrect premise that the statute requires proof of an intent to defraud and the misperception that the HEA imposes no government "supervision and control over the funds after the point of the commingling of the funds." *Ibid.* See 34 C.F.R. 668.23 (audit requirements), 682.605-682.607 (refund requirements).

The indictment in this case alleges facts sufficient to establish that petitioner converted federal loan funds by deliberately failing to refund those funds when due. See Pet. App. A12. Specifically, according to the indictment, petitioner intentionally directed Acme employees not to make refund payments and gave priority to payments for management fees and salary to the Jacksons and Education America over discharging Acme's refund obligations. J.A. 4-5 (¶¶ 4, 11). Petitioner committed those acts despite Acme's mounting refund liability debt, the warnings of Acme's Financial Aid Director, and petitioner's awareness of a school's duty to comply with the requirements under the HEA and the Department of Education's regulations. J.A. 3-5 (¶¶ 4-5, 8, 10, 12). Those allegations clearly set forth facts establishing the "use in an unauthorized manner or to an unauthorized extent of property placed in one's custody for limited use." *Morissette*, 342 U.S. at 272.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

WALTER DELLINGER
Acting Solicitor General
JOHN C. KEENEY
Acting Assistant Attorney General
MICHAEL R. DREEBEN
Deputy Solicitor General
LISA SCHIAVO BLATT
Assistant to the Solicitor General
DANIEL S. GOODMAN
Attorney

JUNE 1997

Section 1097 of Title 20 (1988) provides:

§ 1097. Criminal penalties

(a) In general

Any person who knowingly and willfully embezzles, misapplies, steals, or obtains by fraud, false statement, or forgery any funds, assets, or property provided or insured under [Title IV] shall be fined not more than $10,000 or imprisoned for not more than 5 years, or both; but if the amount so embezzled, misapplied, stolen, or obtained by fraud, false statement, or forgery does not exceed $200, the fine shall not be more than $1,000 and imprisonment shall not exceed one year, or both.

(b) Assignment of loans

Any person who knowingly and willfully makes any false statement, furnishes any false information, or conceals any material information in connection with the assignment of a loan which is made or insured under [Title IV] shall, upon conviction thereof, be fined not more than $1,000 or imprisoned not more than one year, or both.

(c) Inducements to lend or assign

Any person who knowingly and willfully makes an unlawful payment to an eligible lender under part B of this subchapter as an inducement to make, or to acquire by assignment, a loan insured under that part shall, upon conviction thereof, be fined not more than $1,000 or imprisoned not more than one year, or both.

(d) Obstruction of justice

Any person who knowingly and willfully destroys or conceals any record relating to the provision of assistance under [Title IV] with intent to defraud the United States or to prevent the United States from enforcing any right obtained by subrogation under this part, shall upon conviction thereof, be fined not more than $10,000 or imprisoned not more than 5 years, or both.

Supreme Court, U.S.
FILED
JUL 24 1997
CLERK

No. 96-7185

IN THE
Supreme Court of the United States
OCTOBER TERM, 1996

GARRIT BATES,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

---

REPLY BRIEF FOR THE PETITIONER

C. RICHARD OREN
(Appointed by this Court)
1104 Main Street
P.O. Box 532
Rochester, Indiana 46975
(219) 223-9485
Attorney for Petitioner

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

8 pp

QUESTION PRESENTED

Must the United States of America prove fraudulent intent on the part of the defendant, Garrit Bates, as an essential element of the crime of knowingly and willfully misapplying federally insured funds, proscribed by 20 U.S.C. § 1097(a)

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
TABLE OF AUTHORITIES	iv
SUMMARY OF REPLY ARGUMENT	1
REPLY ARGUMENT	1
A. The position of the Government is inconsistent in its analysis of the essential elements of "knowing and willful misapplication"	1
B. The Government's position is inconsistent by acknowledging that misapplication is a species of conversion while admitting that the conduct with which Mr. Bates is charged is a failure to make refunds	3
C. The Government is inconsistent and inaccurate in its description of the factual allegations of the indictment	4
CONCLUSION	5

TABLE OF AUTHORITIES

Cases Page

UNITED STATES SUPREME COURT

Ratzlaf v. United States, 510 U.S. 135 (1994)..... 4

SUMMARY OF REPLY ARGUMENT

Mr. Bates responds to the argument posited by the Government in its brief on the merits by demonstrating that the Government's position is internally inconsistent in at least Three (3) significant aspects: (1) by admitting that to establish a knowing and willful misapplication under § 1097(a) an awareness of the unauthorized nature of the use of funds *and* intentional conduct must be shown, yet continuing to deny that fraudulent intent is an essential element of the offense; (2) by acknowledging that misapplication is a species of conversion focusing on unauthorized *use* of funds, yet admitting that Mr. Bates is actually charged with an error of omission—e.g. a failure to make refunds; and, (3) by overstating allegations of the indictment to foster an appearance that Mr. Bates was alleged to to have actively misused funds. These inconsistencies illustrate the weakness in the government's position and demand a conclusion that fraudulent intent, in addition to conversion, is an essential element of the offense of misapplication of funds as proscribed by 20 U.S.C. § 1097(a). As the indictment failed to identify either essential element by concept or factual allegation, the indictment must be dismissed.

REPLY ARGUMENT

A. The position of the Government is inconsistent in its analysis of the essential elements of "knowing and willful misapplication".

In its brief, the Government states that the "*mens rea* requirement of misapplication under Section 1097(a) is satisfied by knowing and intentional conduct—here, involving consciousness that the use of property is unauthorized." [Gov. Br. p. 23]. The Government also states that the *mens rea* element "knowingly and willfully" . . . "requires only that the defendant be aware that his use of the funds is unauthorized or wrongful and that he act intentionally." [Gov. Br. p. 15]. Thus, it seems quite

clear that the Government is stating that the essential elements of the crime of misapplication of funds as proscribed by § 1097(a) are:

1. that a defendant be *aware* that a certain *use* of funds is unauthorized or wrongful; and,
2. that the defendant intentionally engaged in the wrongful conduct.

However, the Government then continues to argue that the use of the phrase "knowingly and willfully' . . . "does not connote an intent to injure or defraud." [Gov. Br. p. 18]. This asserts a position which is inconsistent with the essential elements of the offense set forth by the Government and is simply placing verbage over substantive analysis.

Mr. Bates has always maintained that misapplication of funds proscribed by § 1097(a) contains the essential elements of (1) conversion (i.e. unauthorized use of funds); and, (2) fraudulent intent. The essential elements of the offense as set forth by the Government in its brief are identical to those asserted by Mr. Bates, with the sole exception that a prime indicator of fraudulent motive (*awareness* of unauthorized or wrongful use) is coupled with unauthorized use as the first essential element of the offense. The analysis championed by Mr. Bates would simply require an initial determination that there was in fact an unauthorized use of funds which occurred; and, if the answer was yes, then require a determination that the unauthorized use was a result of fraudulent intent or wrongful purpose. Evidence that would lead a trier of fact to conclude that a defendant has consciously engaged in the conduct knowing that the *use* of funds was unauthorized would most certainly serve to aid in establishing fraudulent intent. Thus, the assertion by the Government that "knowingly and willfully" does not connote an intent to injure or defraud is rendered meaningless by the Government's own statement of the essential elements of misapplication of funds proscribed by § 1097(a).

B. The Government's position is inconsistent by acknowledging that misapplication is a species of conversion while admitting that the conduct with which Mr. Bates is charged is a failure to make refunds.

The Government acknowledges that misapplication under Section 1097(a) is a species of conversion and argues, correctly, that misapplication involves the unauthorized *use* of funds provided and insured by the United States. [Gov. Br. pp. 14-15].

Throughout the course of these proceedings, Mr. Bates has maintained that the Twelve (12) Counts of the indictment against him were not unambiguously stated inasmuch as these charges merely stated that Mr. Bates did knowingly and willfully misapply funds in a given amount on a given date. Since the term misapply is intrinsicly vague, (in that HEA funds could theoretically be used in numerous ways which may be unauthorized) and the indictment did not otherwise state the essential elements of the offense, Mr. Bates has argued that the indictment was deficient and subject to dismissal. In its brief before this Court, the Government *for the first time acknowledges*, in writing, that Mr. Bates is, in fact, being charged with a failure to make refunds. [Gov. Br. p. 21 n. 12].

What the Government ignores, by asserting both positions, is the fact that a "failure to make refunds" is *not an active use* of funds provided or insured by the United States *but an omission* alleged to have been committed by the petitioner. An allegation that the defendant made an error of omission regarding the funds says nothing about how the funds provided and insured by the United States were actually used by Mr. Bates during the period of time he was making decisions as to which debts of Acme were to be addressed first. It is Mr. Bates firm belief that every use he made of HEA funds during this period was an authorized use and that any failure of Acme to fully meet its refund liability was not the result of any unauthorized use of HEA funds during the period

when he exercised decision making authority over the use of said funds. Thus, the Government has brought charges against Mr. Bates which he cannot defend because the ultimate conduct of which the Government complains does not, of itself, constitute the statutory offense with which he is charged. As set forth in his opening brief, Mr. Bates contends that had the conduct of which the Government complains, (failure to make refunds) constituted, in and of itself, the offense of misapplication of funds in violation of § 1097(a), then the 1992 Amendment of the statute by Congress would have been unnecessary and entirely superfluous. This Court should not construe a statute in a manner as to render an act of Congress totally without meaning. See, *Ratzlaf v. United States*, 510 U.S. 135 (1994).

C. The Government is inconsistent and inaccurate in its description of the factual allegations of the indictment.

In an apparent effort to bolster its position by leading the Court to believe that conversion and fraudulent intent on the part of Mr. Bates could be inferred from the indictment, the Government has overstated the factual allegations of the indictment.

In its brief, the Government states that "[p]etitioner also determined that payments to the Jacksons and Education America would be given priority over making refund payments to lenders following student withdrawals." [Gov. Br. p. 5]. Further, the Government states, that "[s]pecifically, according to the indictment, petitioner intentionally directed Acme employees not to make refund payments and gave priority to payments for management fees and salary to the Jacksons and Education America over discharging Acme's refund obligations." [Gov. Br. p. 33]. As a basis for these statements, the Government has referred to pages 4 and 5 of the Joint Appendix.

Mr. Bates submits that nothing in the indictment (set forth in its entirety in the Joint Appendix, pages 2 through

12) alleges that Mr. Bates ever made payments to Education America or the Jacksons for management fees and salary while making day to day decisions as to which bills of Acme were to be first paid. The pertinent portion of the indictment merely states that Bates "had an understanding with the Jacksons that payments to the Jacksons and/or Education America and other bills took priority over payments of refunds." [J.A. p. 5]. Mr. Bates submits this sentence in the indictment does not allege that he, in fact, made any payments from Acme funds to Education America or the Jacksons. If any such payment had actually occurred, the Government easily could have plainly and unambiguously set forth such an allegation. Mr. Bates submits that the Government did not, and could not in good faith, make such an allegation.

Accordingly, this Court should not conclude, based on the statements in the Government's brief, that Mr. Bates was alleged to have made unauthorized use of funds provided and insured by the United States or that Mr. Bates harbored any fraudulent intent in so doing.

CONCLUSION

For the foregoing reasons, as well as the reasons set forth in the opening brief of the Petitioner, the judgment of the United States Court of Appeals for the 7th Circuit should be vacated and the indictment of Mr. Bates dismissed.

Respectfully submitted,

C. RICHARD OREN
(Appointed by this Court)
1104 Main Street
P.O. Box 532
Rochester, Indiana 46975
(219) 223-9485
Attorney for Petitioner

Supreme Court, U.S.
FILED
APR 25 1997
CLERK

(8)

No. 96-7185

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1996

GARRIT BATES,
Petitioner,
v.
UNITED STATES OF AMERICA,
Respondent.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

BRIEF OF *AMICUS CURIAE* THE NATIONAL ASSOCIATION OF CRIMINAL DEFENSE LAWYERS IN SUPPORT OF PETITIONER

ELLEN YANKIVER SUNI
Professor of Law
University of Missouri-
Kansas City School of Law
5100 Rockhill Road
Kansas City, MO 64110
(816) 235-2372

W. BRIAN GADDY
WYRSCH HOBBS MIRAKIAN
& LEE, P.C.
1101 Walnut St., 13th Fl.
Kansas City, MO 64106
(816) 221-0080

LISA B. KEMLER
(Counsel of Record)
ZWERLING & KEMLER, P.C.
108 N. Alfred St.
P.O. Box 20900
Alexandria, VA 22313
(703) 684-8000

Counsel for Amicus Curiae
National Association of
Criminal Defense Lawyers

19 pp

QUESTION PRESENTED

DID THE INDICTMENT IN THIS CASE PROPERLY CHARGE A WILLFUL MISAPPLICATION OF FUNDS IN VIOLATION OF 20 U.S.C. § 1097(a) WHERE IT FAILED TO ALLEGE THE ESSENTIAL ELEMENT OF INTENT TO DEFRAUD?

TABLE OF CONTENTS

QUESTION PRESENTED i

TABLE OF AUTHORITIES iii

INTEREST OF *AMICUS CURIAE* 1

SUMMARY OF ARGUMENT 2

ARGUMENT:

THE INDICTMENT IN THIS CASE DID NOT PROPERLY CHARGE A WILLFUL MISAPPLICATION OF FUNDS IN VIOLATION OF 20 U.S.C. § 1097(a) IN THAT IT FAILED TO ALLEGE THE ESSENTIAL ELEMENT OF INTENT TO DEFRAUD. 5

A. WHERE, AS HERE, A TERM HAS SETTLED MEANING, CONGRESS IS PRESUMED TO ADOPT THAT MEANING WHEN IT USES THE TERM. . 5

B. WILLFUL MISAPPLICATION HAS HISTORICALLY REQUIRED AN INTENT TO DEFRAUD, WHETHER OR NOT SUCH INTENT IS EXPRESSLY SPECIFIED ON THE FACE OF THE STATUTE. 6

C. USING THE SETTLED MEANING OF WILLFUL MISAPPLICATION IN § 1097 SERVES THE IMPORTANT PURPOSE, FREQUENTLY RECOGNIZED BY CONGRESS AND THIS COURT, OF PREVENTING CONVICTION FOR INNOCENT MISSTEPS. 10

CONCLUSION 13

TABLE OF AUTHORITIES

FEDERAL CASES

Albernaz v. United States,
450 U.S. 333 (1981) 10

Cannon v. University of Chicago,
441 U.S. 677 (1979) 9

Goodyear Atomic Corp. v. Miller,
486 U.S. 174 (1988) 9

Liparota v. United States,
471 U.S. 419 (1985) 10, 11

Morissette v. United States,
342 U.S. 246 (1952) 9, 10

Seals v. United States,
221 F.2d 243 (8th Cir. 1955) 7

United States v. Britton,
107 U.S. 655 (1883) 11

United States v. Christo,
614 F.2d 486 (5th Cir. 1980) 11, 12

United States v. Garcia,
751 F.2d 1033 (9th Cir. 1985) 7

United States v. Kammer,
1 F.3d 1161 (11th Cir. 1993) 11

United States v. Logsdon,
132 F. Supp. 3 (W.D. Ky. 1955), aff'd, 253 F.2d 12 (6th Cir. 1958) 7

United States v. Matot,
146 F.2d 197 (2d Cir. 1944) 8

United States v. Ratzlaf,
510 U.S. 135 (1994) 11

United States v. Schnitzer,
942 F. Supp. 323 (S.D. Tex. 1976) 12

United States v. Vannatta,
189 F. Supp. 937 (D. Haw. 1960) 7

United States v. Wells,
117 S. Ct. 921 (1997), quoting *Nationwide Mutual Insurance Co. v. Darden*, 503 U.S. 318 (1992) 5

United States v. X-Citement Video,
115 S. Ct. 464 (1994) 10

STATE CASES

Louis Pizitz Dry Goods Co. v. Fidelity & Deposit Co. of Md.,
136 So. 800 (Ala. 1931) 9

Maryland Casualty Co. v. Farmers State Bank & Trust Co.,
258 S.W. 584 (Tex. Ct. App. 1924) 9

Roseville Trust Co. v. American Surety Co. of N.Y.,
103 A. 182 (N.J. 1918) 9

FEDERAL STATUTES

12 U.S.C. § 592 6

18 U.S.C. § 656 ..... 3, 6, 7, 11

Ch. 106, § 55, 13 Stat. 116 (1864) 6

20 U.S.C. § 1097(a) 1, 2, 5, 6, 7

TREATISES AND OTHER AUTHORITIES

Appleman, INSURANCE LAW AND PRACTICE, § 5670 (1981) 8

COUCH ON INSURANCE, § 46:67 (2d ed. 1982) 8

Thomas Morse, *Bank Insiders and the Willful Misapplication Statute: Toward a More Effective Protection from Self Dealing*, 92 Banking L.J. 715, 722 n.19 (1975) 6

No. 96-7185

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1996

GARRIT BATES,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

BRIEF OF *AMICUS CURIAE* THE NATIONAL ASSOCIATION OF CRIMINAL DEFENSE LAWYERS IN SUPPORT OF PETITIONER

INTEREST OF *AMICUS CURIAE*[1]

The National Association of Criminal Defense Lawyers ("NACDL") of the District of Columbia is a non-profit

---

[1] The parties have consented to the filing of this Brief by the National Association of Criminal Defense Lawyers. Their letters of consent have been separately filed with the Clerk of the Court concurrently with the filing of this Brief.

corporation with a membership of more than 8,700 attorneys and 28,000 affiliate members, including representatives from all 50 states. The American Bar Association recognizes NACDL as an affiliate organization and awards it full representation in the House of Delegates.

NACDL was founded in 1958 to promote study and research in the field of criminal defense law; to disseminate and advance knowledge of the law in the area of criminal practice; and to encourage integrity, independence, and expertise of defense lawyers. Among NACDL's stated objectives is the promotion of the proper administration of justice. Thus, the members of NACDL have a vital interest in insuring that the integrity of the federal and state systems of criminal justice are protected.

NACDL's interests necessarily include cases dealing with the construction of federal criminal statutes, issues regarding *mens rea*, and the effect of these issues on future prosecutions. Its interests in this case extend to insuring that the proper scienter requirement in prosecutions pursuant to 20 U.S.C. § 1097(a) is alleged and proved when the government elects to proceed under that statute.

SUMMARY OF ARGUMENT

NACDL supports the petitioner's arguments and the decision of the district court below that dismissed the indictment for failing to allege intent to defraud as a requisite element of the offense charged. One of the arguments advanced by the petitioner in his opening brief is that Congress's use of the terms "knowingly" and "willfully" in § 1097 would seemingly require the greatest degree of mental culpability, which would be intent to defraud in the context of this particular statute. In addition to the petitioner's arguments, NACDL respectfully offers an

independent but related reason to show why intent to defraud is indeed a requisite element of § 1097.

"Willful misapplication" is a legal term of art that has been specifically defined and construed by numerous courts prior to the enactment of the criminal penalties set forth in § 1097. For example, the history of 18 U.S.C. § 656, which criminalizes the willful misapplication of bank funds, indicates that proof of willful misapplication requires an intent to defraud, even though intent to defraud is not specifically stated in the text of the statute. Numerous appellate courts have reached the same conclusion in construing § 656. Similarly, willful misapplication has been defined in the context of insurance guaranty contract cases to require an intent to defraud. Based upon the various constructions of willful misapplication in the common law that include intent to defraud as a requisite element, Congress is presumed to have incorporated the common law meanings of the term "willful misapplication" in § 1097.

In addition, the intent to defraud element of § 1097 also serves the important purpose of distinguishing maladministration, accounting errors, or mere technical violations of civil regulations from the harsh criminal sanctions associated with criminal misapplication statutes. Due to the inherent risk that a jury may infer criminal intent from a violation of a civil regulation, the requirement that the government must show intent to defraud prevents the use of mere technical violations of civil regulations to improperly obtain a conviction under a criminal statute without a showing of fraudulent intent.

For these reasons, intent to defraud is an essential element of § 1097, and serves the important purpose of preventing convictions for innocent or unwary conduct. The

district court's determination that the indictment in this matter fails to allege intent to defraud as a requisite element of the offense was proper.

ARGUMENT

THE INDICTMENT IN THIS CASE DID NOT PROPERLY CHARGE A WILLFUL MISAPPLICATION OF FUNDS IN VIOLATION OF 20 U.S.C. § 1097(a) IN THAT IT FAILED TO ALLEGE THE ESSENTIAL ELEMENT OF INTENT TO DEFRAUD.

It is well settled that an indictment must allege all essential elements of the crime charged. Intent to defraud is an essential element of the offense of willful misapplication, the offense charged in the instant case. The indictment in this case wholly failed to allege that Defendant Garrit Bates acted with intent to defraud. That failure rendered the indictment insufficient as a matter of law. The district court's decision to dismiss the indictment on this ground was proper.

A. WHERE, AS HERE, A TERM HAS SETTLED MEANING, CONGRESS IS PRESUMED TO ADOPT THAT MEANING WHEN IT USES THE TERM.

It is axiomatic that where Congress uses a term that "has accumulated settled meaning under . . . the common law," this Court will "presume that Congress incorporate[d] the common-law meaning of the term" unless the statute otherwise dictates. *United States v. Wells*, 117 S. Ct. 921, 927 (1997), *quoting Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318, 322 (1992). In enacting 20 U.S.C. § 1097(a), Congress criminalized the willful misapplication of higher education assistance funds. Although Congress did not, in express words, include a requirement that such misapplication be accompanied by an intent to defraud, such a requirement is clearly found in the

settled meaning of the term "willful misapplication" that is used in § 1097. Accordingly, this element must be charged, and failure of the Government to include the "intent to defraud" element in the indictment in this case mandates reversal.

B. WILLFUL MISAPPLICATION HAS HISTORICALLY REQUIRED AN INTENT TO DEFRAUD, WHETHER OR NOT SUCH INTENT IS EXPRESSLY SPECIFIED ON THE FACE OF THE STATUTE.

When Congress chose to criminalize willful misapplication of higher education assistance funds in 20 U.S.C. § 1097, it was not writing on a clean slate. Willful misapplication has been the subject of criminal sanctions since at least 1864, when the term first appeared in the Act of June 3, 1864 as part of the National Bank Act, which provided criminal penalties for embezzlement or willful misapplication of banking association funds. *See* Ch. 106, § 55, 13 Stat. 116 (1864). *See also* Thomas Morse, *Bank Insiders and the Willful Misapplication Statute: Toward a More Effective Protection from Self Dealing*, 92 BANKING L.J. 715, 722 n.19 (1975). At that time, the statute contained an explicit requirement of an intent to defraud.

While the presence of such an explicit requirement in the 1864 statute might be viewed as an indication that intent to defraud is not subsumed or embedded in willful misapplication itself, any thought along those lines was clearly dispelled by the revision of the statute in 1948. Pursuant to a major revision of federal criminal law that year, the statute, previously codified at 12 U.S.C. § 592, was rewritten and moved to its current location in 18 U.S.C. § 656. At that time, the explicit requirement of intent to defraud was dropped from the statutory terms. Any contention that this change in statutory language

was inadvertent or unintentional is belied by the Revisor's Notes accompanying the revision, which explicitly indicate that the "revised section, without changing in any way the meaning or substance of existing law, clarifies, condenses, and combines related provisions largely rewritten in matters of style." Historical and Revisor's Notes, 18 U.S.C.A. § 656.[2] In this revision, Congress retained the offense of willful misapplication of bank funds, but removed any explicit reference to intent to defraud in the text of the statute. Courts interpreting this Congressional revision shortly after it occurred uniformly concluded that the Revisor's Notes meant what they said - - - that proof of willful misapplication still requires a showing of intent to defraud, despite the absence of such language in the statute itself. *See, e.g., Seals v. United States*, 221 F.2d 243, 245 (8th Cir. 1955); *United States v. Vannatta*, 189 F. Supp. 937, 939 (D. Haw. 1960). As expressed by the judge in *United States v. Logsdon*, 132 F. Supp. 3, 5 (W.D. Ky. 1955), *aff'd*, 253 F.2d 12 (6th Cir. 1958), "the words 'with intent . . . to injure or defraud' were undoubtedly omitted from the revised section as being redundant. Their omission does not change or detract from the former meaning of the statute."[3]

---

[2] The Revisor's Notes indicate that the original section contained more than 500 words and was "verbose, diffuse, redundant, and complicated." The changes were designed to maintain the same meaning while doing away with excess words. It is clear that "intent to defraud" was viewed as such an excess.

[3] *See also United States v. Garcia*, 751 F.2d 1033, 1036 (9th Cir. 1985), reaching the same conclusion, that willful misapplication requires an intent to defraud, with regard to a statute that criminalizes a willful misapplication of CETA funds. The court there stated: "The only reason Congress could have considered the explicit requirement of a purpose to injure or defraud redundant was that Congress understood the term 'willful misapplication' to include such an intent by implication." *Id.*

This after-the-fact judicial interpretation is not only consistent with the contemporaneous Revisor's Notes, it also reflects the teaching of one of the best judicial minds of the time shortly prior to the legislative change. Notable is the opinion of Judge Learned Hand, writing for the Second Circuit in *United States v. Matot*, 146 F.2d 197 (2d Cir. 1944), just four years before the statutory change from § 592 to § 656. In *Matot*, Judge Hand, in commenting on the presence of the "intent to defraud" language in § 592, stated his belief that "that construction is unnecessary, for 'willful misapplication' of money presupposes a fraudulent intent . . . ." *Id.* at 198.

Not only do prior and contemporaneous interpretations of § 656 strongly suggest that intent to defraud is an essential component of willful misapplication, subsequent judicial interpretation does so as well. As noted by the author of a comprehensive article on § 656 written in 1975, five years before the enactment of the criminal penalties at issue in this case, "further cases appear to have particularized the intent contemplated by the term [willful misapplication] so that today the required willfulness has become exclusively an intent to injure or defraud . . . ." *Morse*, 92 BANKING L.J., *supra*, at 726 and cases cited (footnote omitted).

This consistent interpretation of "willful misapplication" in criminal statutes to include the element of intent to defraud mirrors a long line of authority in the area of insurance guaranty contracts, the other significant area where the term "willful misapplication" is found. As recognized by both major treatises in insurance law, it is generally held that willful misapplication requires that the acts of conversion "be done with a dishonest or fraudulent intent." Appleman, INSURANCE LAW AND PRACTICE, § 5670 (1981); COUCH ON INSURANCE, § 46:67 (2d ed. 1982). The cases relied on by these treatises to support the implication of an intent to defraud within the meaning of willful

misapplication date from shortly after the turn of the century through the late 1930's. *See, e.g., Louis Pizitz Dry Goods Co. v. Fidelity & Deposit Co. of Md.*, 136 So. 800, 801-02 (Ala. 1931); *Roseville Trust Co. v. American Sur. Co. of N.Y.*, 103 A. 182, 183 (N.J. 1918); *Maryland Casualty Co. v. Farmers' State Bank & Trust Co.*, 258 S.W. 584, 586 (Tex. Ct. App. 1924). These cases were presumptively known to Congress at the time of both its revision of § 656 and its subsequent enactment of § 1097. *See Goodyear Atomic Corp. v. Miller*, 486 U.S. 174, 184-85 (1988); *Cannon v. University of Chicago*, 441 U.S. 677, 698-99 (1979).

The conclusion is thus inescapable that, in using the term "willful misapplication" to criminalize improper use of higher education assistance funds in § 1097, Congress was incorporating the well-settled requirement that such misapplication must be accompanied by an intent to defraud. It is inconceivable that Congress would have used a term with such a long, consistent history of interpretation unless it intended that interpretation to be followed with regard to § 1097. As this Court said in *Morissette v. United States*, 342 U.S. 246, 250 (1952):

> [W]here Congress borrows terms of art in which are accumulated the legal tradition and meaning of centuries of practice, it presumably knows and adopts the cluster of ideas that were attached to each borrowed word in the body of learning from which it was taken and the meaning its use will convey to the judicial mind unless otherwise instructed. In such case, absence of contrary direction may be taken as

> satisfaction with widely accepted definitions, not as a departure from them.

Morissette was decided before the enactment of § 1097, and Congress is presumed to have been aware of that decision at the time it enacted this statute. *Albernaz v. United States*, 450 U.S. 333, 341-42 (1981).

Congress' use of the term "willful . . . misapplication" in § 1097 includes within its clearly understood meaning and interpretation the requirement of an intent to defraud. Such intent was not alleged in the indictment in this case. Accordingly, that indictment was defective and should properly be dismissed.

C. USING THE SETTLED MEANING OF WILLFUL MISAPPLICATION IN § 1097 SERVES THE IMPORTANT PURPOSE, FREQUENTLY RECOGNIZED BY CONGRESS AND THIS COURT, OF PREVENTING CONVICTION FOR INNOCENT MISSTEPS.

It is a basic and well accepted principle that "an injury can amount to a crime only when inflicted by intention." *Morissette*, 342 U.S. at 250. The requirement of *mens rea* in criminal statutes serves to assure that a "broad range of apparently innocent conduct" is not subjected to criminal sanction. *Liparota v. United States*, 471 U.S. 419, 426 (1985). Just as courts will apply a *mens rea* term where necessary to ensure the appropriate level of scienter consistent with congressional intent, *Morissette*, 342 U.S. at 250; *United States v. X-Citement Video*, 115 S. Ct. 464, 468 (1994), so too must scienter requirements be taken seriously where spelled out in the

statute itself. This is especially true where statutes such as § 1097 are involved. As this Court noted in addressing willful misapplication under § 656, where maladministration rather than true misapplication is involved, no criminal sanctions are appropriate. *United States v. Britton*, 107 U.S. 655, 666-67 (1883). In statutes where the risk of prosecuting innocent missteps is great, *Liparota*, 471 U.S. at 426; where the conduct involved is, as here, not so "obviously 'evil' or inherently 'bad,'" *United States v. Ratzlaf*, 510 U.S. 135, 146 (1994); where, as here, failure to rigorously apply the stated mental element can lead to felony sanctions for simple business misjudgment, courts must take special care to ensure that a stated *mens rea* requirement is given full effect.

That concern is particularly acute with regard to § 1097, as illustrated by both *United States v. Kammer*, 1 F.3d 1161 (11th Cir. 1993), and the indictment in this case. In both *Kammer* and here, much of what was alleged against the defendant relates to an alleged failure to adequately comply with civil regulations. Unless willful misapplication is understood to require an intent to defraud, there will be substantial risk that defendants will be criminally sanctioned for mere violations of technical regulations.

The use by the government of a violation of a civil regulation to obtain or "bootstrap" a conviction under a criminal misapplication statute has drawn strong criticism from several courts of appeals. Most notably, the Fifth Circuit has held that the introduction of evidence involving a violation of a civil banking statute in a criminal prosecution under 18 U.S.C. § 656 was wholly improper and impermissibly infected the very purpose of the criminal trial, which was to determine the elements of criminal misapplication under § 656. *United States v. Christo*, 614 F.2d 486, 492 (5th Cir. 1980). The Fifth Circuit noted that evidence of the civil violation improperly shifted the

jury's focus away from the elements of the criminal statute and may have invited it not only to infer criminal intent, but to convict the defendant based solely on the violation of civil law. *Id.* It is well established that violations of civil regulations alone cannot amount to a criminal offense. *United States v. Schnitzer*, 942 F. Supp. 323, 329 (S.D. Tex. 1976).

The grave concerns raised when there is an interplay between civil regulations and a criminal offense are heightened if intent to defraud is not a requisite element of the criminal offense. Without requiring intent to defraud, the chances that a jury may convict an innocent person for maladministration, accounting errors, or the mere violation of civil regulations are enhanced. These concerns are present in this case due to the fact that the indictment refers to the civil regulations governing refunds of student loans. The only way to avoid the untoward result of obtaining a conviction based on a violation of a civil regulation or for poor business judgment is recognition of the requirement of intent to defraud within the meaning of willful misapplication. Intent to defraud serves the purpose of separating purely innocent conduct, such as maladministration or the violation of technical civil regulations, from conduct that is appropriately considered criminal.

CONCLUSION

For the foregoing reasons, the decision of the Seventh Circuit Court of Appeals should be vacated and reversed and the district court's decision that dismissed the indictment for failure to allege a requisite element should be affirmed.

Respectfully submitted,

LISA KEMLER
(Counsel of Record)
ZWERLING & KEMLER, P.C.
108 N. Alfred St.
P.O. Box 20900
Alexandria, VA 22314
(703) 684-8000

PROFESSOR ELLEN YANKIVER SUNI
University of Missouri- Kansas City
School of Law
5100 Rockhill Rd.
Kansas City, MO 64110
(816) 235-2372

W. BRIAN GADDY
WYRSCH HOBBS MIRAKIAN
& LEE, P.C.
1101 Walnut St., 13th Fl.
Kansas City, MO 64106
(816) 221-0080
Counsel for Amicus Curiae
National Association of
Criminal Defense Lawyers

April 24, 1997